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11 UNITED STATES DISTRICT COURT
12
13 NORTHERN DISTRICT OF CALIFORNIA

14 WILLIAM LAMARTINA, Individually and on)
Behalf of All Others Similarly Situated,)
15 Plaintiff,)

16 vs.)

17 VMWARE, INC., et al.,)

18 Defendants.)
19

Case No. 5:20-cv-02182-EJD

CLASS ACTION

CONSOLIDATED COMPLAINT FOR
VIOLATIONS OF THE FEDERAL
SECURITIES LAWS

DEMAND FOR JURY TRIAL

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1 Lead Plaintiff Northeast Carpenters Pension Fund (“Lead Plaintiff”) by and through its
 2 undersigned counsel, brings this federal class action based upon personal knowledge as to those
 3 allegations concerning itself and, as to all other matters, upon the investigation of counsel, which
 4 included, without limitation, the review and analysis of: (a) public filings made by VMware, Inc.
 5 (“VMware” or the “Company”) with the U.S. Securities and Exchange Commission (the “SEC”); (b)
 6 releases and other publications disseminated by defendants; and (c) securities analyst reports, news
 7 articles, websites and other publicly available information concerning defendants.¹ Lead Plaintiff
 8 believes that substantial additional evidentiary support will likely exist for the allegations set forth
 9 herein after a reasonable opportunity for discovery.

10 **I. INTRODUCTION**

11 1. This is a federal securities class action on behalf of a Class (defined herein) consisting
 12 of all persons other than defendants who purchased or otherwise acquired VMware securities
 13 between August 24, 2018, and February 27, 2020, both dates inclusive (the “Class Period”), seeking
 14 to recover damages caused by defendants’ violations of the federal securities laws and to pursue
 15 remedies under §§10(b), 20(a) and 20A of the Securities Exchange Act of 1934 (the “Exchange
 16 Act”) and Rule 10b-5 promulgated thereunder, against the Company and certain of its officers.

17 2. Defendants violated the federal securities laws by deceptively recording sales as
 18 backlog so that the revenue from those sales could be recognized in subsequent quarters as opposed
 19 to the quarter when they were actually made. In order to meet and not overly exceed market
 20 expectations, once quarterly sales goals were achieved, management directed the Company’s
 21 personnel to hold secured contracts until the next quarter, resulting in revenue smoothing into
 22 subsequent quarters, causing reported revenue to be far more consistent across reporting periods than
 23 it actually was. This deliberate smoothing of revenue artificially inflated backlog reported to
 24 investors and created an impression of steady sales that was not indicative of actual corporate
 25 performance.

26
 27 ¹ “Defendants” collectively refer to VMware, Patrick P. Gelsinger and Zane Rowe. “Individual
 28 Defendants” refer to defendants Patrick P. Gelsinger and Zane Rowe.

1 3. Defendants materially and artificially inflated backlog using sales that were not
2 required to meet current period guidance throughout Fiscal Year (“FY”) 2019, and particularly at
3 year end, misleading investors as to the likelihood that FY 2020 guidance would be met. Defendants
4 treated the inflated backlog – nearly half a billion dollars at the end of FY 2019 – as a slush fund,
5 drawing on it throughout FY 2020 rather than recognizing the revenue in FY 2019. By deferring
6 revenue recognition to FY 2020, VMware was able to continue to deliver double digit earnings
7 growth in FY 2020. Had VMware recognized the revenue that was deferred into backlog during FY
8 2019, when it was in fact secured, VMware would have delivered only low single digit revenue
9 growth for FY 2020.

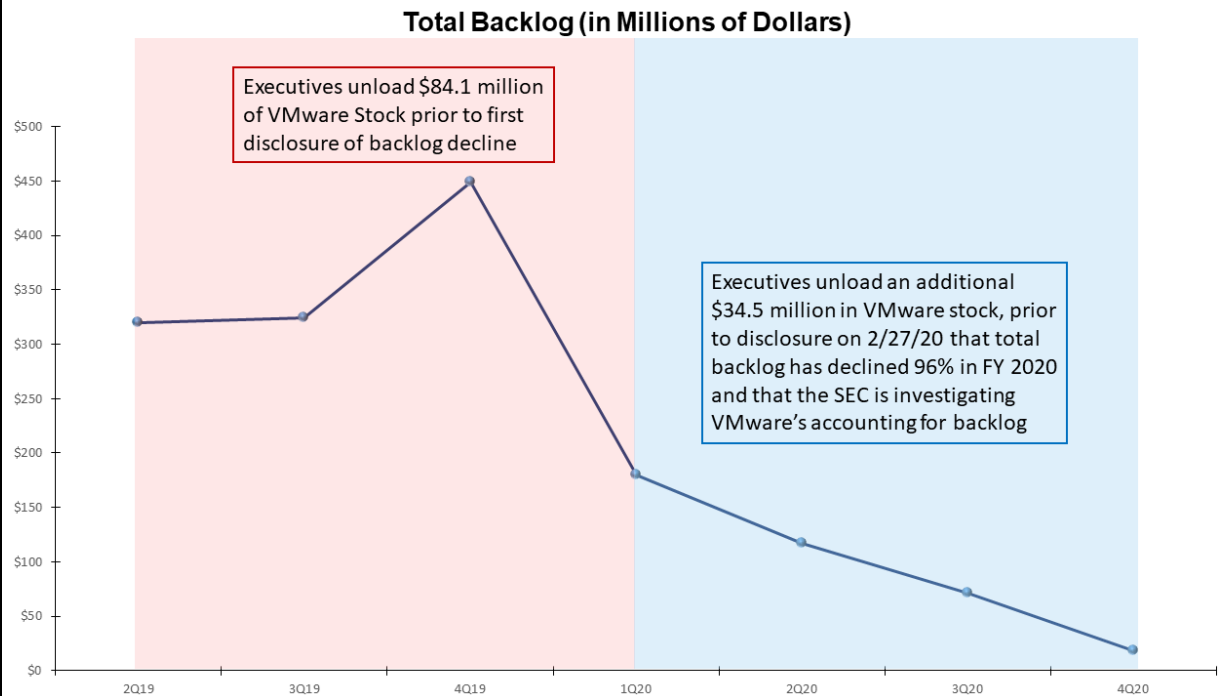
10 4. Backlog is an important metric to investors, as it helps inform their predictions of
11 future revenue. Because stocks are valued, in large part, based upon future cash flows and growth
12 potential as opposed to past earnings, the inflation of backlog and the smoothing of revenue and
13 earnings inflated VMware’s stock price during the Class Period. As a result of the inflated backlog
14 and smoothing of revenue, the notes to VMware’s financial statements during the Class Period
15 violated Generally Accepted Accounting Principles (“GAAP”) because they failed to disclose to
16 investors sufficient information to help them understand the timing and uncertainty of the
17 Company’s projected and later, reported revenue.

18 5. The inflated backlog was also used to conceal the fact that VMware was plagued by
19 weaknesses heading into FY 2020 driven by an: (i) internal segment reorganization; and (ii)
20 VMware’s failure to properly weather an industry-wide shift away from license products in favor of
21 subscription and Software-as-a-Service (“SaaS”) products.

22 6. The practice of deceptively pushing current quarter sales into future quarters inflated
23 reported backlog and gave investors a false impression of the true state of the Company’s FY 2020
24 growth and growth prospects. A series of quarterly disclosures in FY 2020 began to reveal the true
25 state of VMware’s far lower backlog, culminating on February 27, 2020, when the Company
26 revealed that: (1) VMware’s total backlog had declined 96% from its height just one year prior; (2)
27 VMware poorly managed the industry-shift to subscription and SaaS products; and (3) VMware
28 could not meet Q4 2020 or FY 2020 revenue guidance issued just three months prior. The same day,

VMware also announced that in December 2019, the SEC launched an investigation into the Company's backlog and associated accounting and disclosures, on the heels of the sudden resignation of the Company's Chief Accounting Officer.

7. VMware's stock price dropped swiftly and dramatically in the trading days following each partial disclosure as market participants recalibrated expectations as a result of declining backlog and slower than expected growth. In total, the value of VMware shares declined \$85 per share – over 41% from its Class Period high in just nine months. From the start of the Class Period until the Company's February 27, 2020 disclosures, the Company's executives, including the Individual Defendants, took advantage of the Company's artificially inflated stock price, unloading over \$118 million of VMware stock at inflated prices as detailed in the figure below, and at ¶¶126-136:



II. JURISDICTION AND VENUE

8. The claims asserted herein arise under and pursuant to §§10(b), 20(a), and 20A of the Exchange Act (15 U.S.C. §§78j(b), 78t(a), and 78t-1), and SEC Rule 10b-5 promulgated thereunder by the SEC (17 C.F.R. §240.10b-5).

1 9. This Court has jurisdiction over the subject matter of this action under 28 U.S.C.
2 §1331 and §27 of the Exchange Act (15 U.S.C. §78aa).

3 10. Venue is proper in this Judicial District pursuant to §27 of the Exchange Act (15
4 U.S.C. §78aa) and 28 U.S.C. §1391(b). VMware is headquartered in this Judicial District,
5 defendants conduct business in this Judicial District, and a significant portion of defendants'
6 activities took place within this Judicial District.

7 11. In connection with the acts alleged herein, defendants, directly or indirectly, used the
8 means and instrumentalities of interstate commerce, including, but not limited to, the mails,
9 interstate telephone communications, and the facilities of the national securities markets.

10 **III. THE PARTIES**

11 **Plaintiff**

12 12. Lead Plaintiff Northeast Carpenters Pension Fund is a defined benefit pension plan
13 with assets of over \$2.5 billion that provides retirement benefits to over 35,000 participants. Lead
14 Plaintiff purchased VMware shares and was damaged thereby as detailed in the Certification
15 Pursuant to Federal Securities Laws, attached hereto.

16 **Defendants**

17 13. VMware is incorporated in Delaware with principal executive offices located at 3401
18 Hillview Avenue in Palo Alto, California. VMware's common stock trades on the NYSE under the
19 ticker symbol "VMW."

20 14. Patrick P. Gelsinger ("Gelsinger") served as VMware's Chief Executive Officer
21 ("CEO") during the Class Period. During the Class Period, Gelsinger sold \$23.4 million worth of
22 VMware stock at inflated prices while in the possession of material nonpublic information, including
23 shares sold contemporaneously with Lead Plaintiff's purchase of shares in March 2019.

24 15. Zane Rowe ("Rowe") served as VMware's Chief Financial Officer ("CFO") and
25 Executive Vice President during the Class Period. During the Class Period, Rowe sold \$17.8 million
26 worth of VMware stock at inflated prices while in the possession of material nonpublic information.

1 **IV. OVERVIEW OF THE CASE**

2 **A. Background of the Company**

3 16. VMware is a software and technology firm based in Palo Alto, California. The
4 Company provides application modernization and cloud computing and virtualization software and
5 services for its customers throughout the world. VMware enables its customers to digitally
6 transform their operations by allowing businesses to more efficiently use existing hardware
7 capabilities by allowing network components, such as servers, to run multiple operating systems or
8 host multiple dedicated applications simultaneously.

9 17. VMware operates in three market segments: Americas (comprised of Latin America,
10 United States, and Canada), Asia Pacific & Japan (“APJ”) and Europe Middle East and Africa
11 (“EMEA”). Throughout the Class Period, defendants regularly touted ““broad-based strength across
12 our diverse product portfolio and in all three geographies,”” signaling to investors that all three of the
13 Company’s operating segments – Americas, APJ, and EMEA – were experiencing periods of
14 continued strength.

15 18. VMware’s product offerings include licenses, subscription and SaaS, and services.
16 During the Class Period, VMware derived revenue primarily from licensing software under perpetual
17 licenses or consumption-based contracts and the related service revenue, which was comprised of
18 software maintenance and support, training, consulting services and hosted services. License
19 revenue is revenue the Company generates from selling license software through distributors,
20 resellers, system vendors, system integrators and its direct sales force. VMware’s subscription and
21 SaaS revenue consists of hosted services, license usage fees, and perpetual or subscription license
22 sales of its software platform. VMware’s on-premises license revenue is recognized up front at a
23 point in time, upon delivery and transfer of control of the underlying license to the customer, or upon
24 point-of-sale to the end user. License revenue is also recognized upon consumption for rental fees of
25 VMware’s rental of on-premises licenses. In contrast, subscription and SaaS revenue is recognized
26 on a ratable basis over the contract term generally beginning on the date the software is delivered to
27 the customer, and thus, is recognized more slowly than license revenue.

1 19. During the Class Period, the Company only reported two revenue line items: license
2 and services. Subscription and SaaS revenue was allocated between the license and services line
3 items, with the bulk of subscription and SaaS revenue allocated to licenses. At the end of the Class
4 Period, beginning with its FY 2020 Form 10-K, VMware began reporting subscription and SaaS
5 revenue as a separate line item, to align with industry demands, as the industry shifted away from
6 license products in favor of subscription and SaaS and to provide a more meaningful representation
7 of the nature of the Company's revenue.

8 20. The Company recognized revenue as it performed its obligations on existing deals.
9 Deals that were made in one quarter, but that the Company expected to deliver and recognize in
10 revenue the next quarter, were included in the Company's "backlog." Thus, backlog is a
11 representation of sales that were already secured, but were not yet fulfilled by the Company –
12 revenue for deals in the Company's pipeline would be recognized as the Company performed its
13 obligations related to its backlog the subsequent quarter. In addition to total backlog, the Company
14 also separately disclosed the portion of backlog attributable to licenses.

15 21. Backlog is an important measure of the Company's existing product demand and
16 expected future cash flows and revenue. Healthy backlog signaled to investors that the Company
17 was experiencing robust client demand, as it was a measure of the Company's existing deal pipeline
18 and quantified the amount of product that had been ordered by VMware's customers, but that had yet
19 to be fulfilled as of quarter end. Analysts and investors considered backlog a key performance
20 indicator because it essentially gave the Company a "head start" to meeting revenue and earnings
21 targets for the subsequent financial reporting period.

22 **B. Defendants Materially and Artificially Inflated Backlog to Conceal**
23 **the True State of VMware's Business**

24 22. Throughout FY 2019, and particularly at fiscal year end, defendants engaged in a
25 practice of materially and artificially inflating both license and total backlog by pushing sales that
26 were not required to meet current period revenue or earnings guidance because guidance had already
27 been met from the current quarter into the next quarter, by deliberately leaving them categorized as
28 unfulfilled at quarter end.

23. Sales personnel would submit executed contracts for processing through the systems operations group at VMware's headquarters. At the end of each quarter, and particularly at year end, VMware would deliberately leave executed contracts unprocessed, to be recognized in the subsequent quarter by funneling them into the Company's backlog. This practice served no legitimate purpose and had the effect of delaying and smoothing the recognition of revenue so that the revenue from those contracts would be recognized the next quarter rather than the quarter in which the contract execution was achieved.

24. By pushing sales not required to meet FY 2019 guidance into FY 2020, VMware was able to report a head start – *nearly half a billion dollars* – toward meeting revenue guidance for FY 2020. This gave analysts and investors a false impression that VMware would be able to meet FY 2020 guidance, and created the perception of a state of affairs at VMware that was dramatically different from what actually existed at the start of FY 2020. By deferring revenue recognition to FY 2020, VMware was able to continue to deliver double digit revenue growth in FY 2020. Had VMware recognized the revenue that was deferred into backlog during FY 2019 when it was in fact secured, VMware would have delivered only low single digit revenue growth for FY 2020.

25. During each quarter of FY 2019, the Company reported dramatic increases in total backlog. For FY 2019, the Company reported a 58% increase in total backlog, from \$285 million at the beginning of the year, to \$449 million at year end. During the same period, license backlog likewise increased 48% from \$99 million at the start of FY 2019 to \$147 million at the end of FY 2019.

26. The dramatic increases in backlog the Company experienced during FY 2019, and particularly at year end, indicated to investors that the Company had a solid head start to meet publicly communicated double digit revenue growth guidance for FY 2020. As defendants advanced a story of impressive growth and success in booking deals with customers that VMware would fulfill in subsequent quarters, the Company's stock price soared, as the market reacted positively to the increases in backlog each quarter in FY 2019. VMware stock ultimately reached a Class Period high of \$205.52 on May 16, 2019, just two weeks prior to the release of the Company's Q1 2020 results,

1 the first quarter in which VMware began to draw down on its backlog slush fund in order to meet
2 guidance.

3 27. Defendants' motivation for racking up substantial backlog was two-fold. First, once
4 guidance was met in FY 2019, VMware management directed that sales be deferred from the current
5 period and recorded as backlog, so that the revenue would be available to smooth the next quarter
6 and fiscal year results, in order to ensure that publicly communicated guidance that had been
7 provided to investors could be met. This practice enhanced the Company's prospects of meeting
8 guidance and analyst expectations in future periods, and led investors to believe that VMware's
9 license and total revenue guidance would be met in FY 2020. By deferring revenue recognition to
10 FY 2020, VMware was able to continue to deliver double digit revenue growth in FY 2020. Had
11 VMware recognized the revenue that was deferred into backlog during FY 2019, when it was in fact
12 secured, VMware would have delivered only low single digit revenue growth for FY 2020.

13 28. Second, pushing sales into backlog also allowed the Company to meet current period
14 revenue targets while at the same time capping the current period baseline upon which future
15 revenue growth would be measured. Recognizing the backlog sales organically in the quarter in
16 which they were secured rather than pushing them out into the subsequent quarter would have meant
17 that analyst growth expectations in FY 2020 would have been harder to meet, as achieving the same
18 percentage growth would have required nearly a *half a billion more* in total revenue if the backlog
19 sales had been recognized in FY 2019.

20 29. Defendants' practice of deceptively pushing sales into backlog concealed from
21 investors and the market several issues that would plague the Company in FY 2020: (i) a poorly
22 performing Americas segment following a reorganization in that region; and, (ii) a failure to
23 successfully weather the industry-wide shift away from license products in favor of subscription and
24 SaaS products. During FY 2020, VMware drew down on its backlog slush fund in order to continue
25 to conceal the impact of these adverse business conditions.

26 30. Unbeknownst to investors, VMware was facing several challenges that jeopardized
27 the Company's ability to meet revenue guidance. VMware's Americas segment was in a state of
28 turmoil – just days after the close of FY 2019 in February 2019, VMware saw the departure of its

1 head of Americas segment, leading to the reorganization of the Americas region and appointment of
2 a new Americas leader. This realignment resulted in deal execution problems and a subsequent
3 slowdown in revenue following weakened performance in that region. Defendants failed to disclose
4 this restructuring during the Q4 2019 conference call on February 28, 2019, instead three months
5 later, defendants relayed to analysts that the restructuring of the Company's Americas segment
6 caused "disruption" and that some of the Company's "deals were impacted."

7 31. Separately, as customers' consumption of software evolved, the Company was failing
8 to address the industry-shift away from its license model, which was becoming obsolete, to
9 subscription and SaaS products, which slowed the timing of revenue recognition and negatively
10 impacted the Company's revenue growth. Notwithstanding this industry trend, defendants falsely
11 assured the market that VMware's performance and pipeline were on track to deliver expected
12 results throughout FY 2020, thanks in part, to its ability to generate strong license backlog and
13 revenue growth.

14 32. In order to cushion the negative impact these events would have had on the
15 Company's financial performance in FY 2020, defendants poured excess FY 2019 sales into
16 VMware's backlog throughout FY 2019, thus artificially inflating backlog and misleading investors
17 as to VMware's prospects for FY 2020 and creating a lower threshold to measure future growth. As
18 a result of their practice of deliberately pushing sales into backlog, defendants were aware, but failed
19 to disclose, that backlog was no longer an accurate barometer of the Company's expected
20 performance.

21 33. VMware's notes to the Class Period consolidated financial statements were
22 inadequate in violation of GAAP. VMware disclosed in its SEC filings that "[t]he consolidated
23 financial statements and accompanying notes have been prepared in accordance with accounting
24 principles generally accepted in the United States of America ('GAAP') and pursuant to the rules
25 and regulations of the [SEC] for annual financial reporting." (2019 10-K at 65). However,
26 VMware's "Revenue Recognition" note failed to disclose to investors sufficient information to
27 understand the timing and uncertainty of revenue, in violation of Financial Accounting Standards
28

1 Board (“FASB”) Accounting Standards Codification (“ASC”) Topic 606, Revenue from Contracts
2 with Customers.

3 34. The objective of the GAAP disclosure requirements “is for an entity to disclose
4 sufficient information to enable users of financial statements to understand the nature, amount,
5 timing, and uncertainty of revenue and cash flows arising from contracts with customers,” and to
6 achieve that objective, an entity must disclose qualitative and quantitative information about its
7 contracts and significant judgments. *See* ASC 606-10-50-1. An entity is required to disclose the
8 judgments, and changes in the judgments, made in applying the revenue recognition guidance “that
9 significantly affect the determination of the amount and timing of revenue from contracts with
10 customers,” and in particular, must explain the judgments, and changes in the judgments, used in
11 determining the timing of satisfaction of performance obligations. *See* ASC 606-10-50-17.

12 35. Despite these requirements and unbeknownst to investors, VMware failed to disclose
13 that significant judgments were made to defer recognizing revenue to a subsequent period once
14 guidance had been met. Such judgments caused revenue to be less than it otherwise would have
15 been in FY 2019, and more than it would have been in FY 2020.

16 36. Not only were VMware’s financial footnote disclosures during the Class Period
17 inadequate, but VMware’s Management’s Discussion & Analysis (“MD&A”) disclosures were also
18 inadequate for failing to disclose defendants’ deferral of revenue to subsequent quarters once
19 guidance had been met, in violation of SEC disclosure requirements. VMware’s undisclosed
20 smoothing of earnings materially distorted the Company’s reported results of operations. SEC Staff
21 Accounting Bulletin (“SAB”) 114, Topic 13.B. notes that significant changes in backlog that
22 reasonably might be expected to result in a revenue change the next period should be disclosed and
23 discussed. However, VMware failed to disclose its practice of intentionally deferring revenue to
24 smooth earnings and the impact on its current period results and future financial results. By failing
25 to make the required disclosures in accordance with GAAP and SEC disclosure rules, VMware’s
26 Class Period financial statements and MD&A were misleading.

27 37. Additionally, during the Class Period, defendants continually touted their double digit
28 revenue growth and expected future revenue growth. For example, during the Q4 2019 earnings

call, VMware reported double-digit revenue growth over the prior year and defendant Rowe provided guidance for FY 2020 for total and license revenue growth in the double-digits over FY 2019. Unbeknownst to investors, defendants were planning to achieve such growth rates by deferring revenue to manipulate revenue growth rates. Without the artificial boost to FY 2020 revenue from the deferral of revenue intentionally held as backlog at the end of FY 2019, VMware would have been forced to disclose significantly lower revenues and growth rates in FY 2020. Such information about its revenue practices and impacts were required to be disclosed.

38. The significant financial impact of the earnings manipulation on VMware's future financial results is precisely the type of information required to be disclosed under the SEC's MD&A rules. For example:

MD&A must specifically focus on known material events and uncertainties that would cause reported financial information not to be necessarily indicative of future *operating performance* or of future financial condition.

* * *

One of the principal objectives of MD&A is to provide information about the quality and potential variability of a company's earnings and cash flow, so that readers can ascertain the likelihood that past performance is indicative of future performance.²

39. By deferring revenue to future quarters, VMware was aware that revenue in the current and subsequent quarters would be impacted. As a result, VMware was required to warn investors that its reported revenue was not indicative of future results.

C. Defendants Announce Record-Breaking Backlog Despite a Slowdown in the Industry

40. During the Q4 2019 earnings conference call for analysts and investors on February 28, 2019, defendant Gelsinger remarked that "Q4 was a terrific ending to a strong fiscal '19," with growth "driven by broad-based strength across our diverse product portfolio in all 3 geographies," adding defendants were "very pleased with this terrific quarter and fiscal '19." Defendant Rowe shared those sentiments, claiming "broad-based strength across the business," and "record results in

² SEC Interpretation: *Commission Guidance Regarding Management's Discussion and Analysis of Financial Condition and Results of Operations* (Release Nos. 33-8350; 34-48960; FR-72), Effective Date: December 29, 2003.

both Q4 and fiscal '19 for license revenue.” Commenting on the strength of the Company’s license backlog, Rowe stated that VMware “exited Q4 with \$147 million of license backlog compared to \$144 million at the end of Q3.”

41. Analysts were surprised by the Company’s continued growth through the quarter, as other major technology companies were experiencing slowdowns. One analyst highlighted that VMware was not seeing the same weaknesses as other companies, including VMware’s competitor Nutanix, and sought clarity into the reason for the divergence. In response, inferring that VMware was a “winner” in a market full of “winners and losers,” defendant Gelsinger confirmed that he was “really happy with our performance.”

D. Following the Announcement of Record-Breaking License Backlog, VMware Executives Sell Nearly \$60 Million of VMware Stock at Inflated Prices

42. Knowing that the Company’s massive backlog reported at the close of FY 2019 would be drawn upon and not replenished and thus was no longer an accurate metric regarding the Company’s financial health, VMware’s executives began selling large quantities of their VMware stock, as the share price was inflated to all-time highs.

43. Prior to the disclosure of the Company’s declining license backlog at the end of Q1 2020, Individual Defendants and other executives unloaded millions in VMware stock. From March 1, 2019 – the day immediately following the Company’s Q4 2019 positive earnings announcement (including record license backlog) – through May 2, 2019 – just *one day* prior to the close of Q1 2020 – VMware executives, including the Individual Defendants, unloaded \$58.9 *million* in VMware stock at inflated prices, as high as \$204.83 per share. *See* Figure 2, below.

44. Notably, on March 1, 2019, the day after defendants disclosed record license backlog to end Q4 2019, defendant Gelsinger alone sold over 21,000 shares of VMware stock to yield almost \$3.8 million in proceeds. Lead Plaintiff purchased 396 shares four days later.

45. VMware’s key executives responsible for managing the Company’s day-to-day operations continued to sell millions of dollars of VMware stock prior to each quarterly corrective disclosure – a total of \$118.6 million during the Class Period. *See* §IV.F.

E. Defendants Draw Down the Backlog Slush Fund While Continuing to Falsely Reassure Investors

46. During the Company's Q1 2020 earnings call on May 30, 2019, just two weeks after VMware's stock price hit all-time highs following a remarkable end to FY 2019, defendants disclosed a drastic decline to the Company's license backlog. At the close of Q1 2020, VMware's license backlog fell **over 67%** from Q4 2019 to end at just \$48 million. The same day, defendants revealed that VMware's Americas segment saw the departure of its leader in February 2019 and as a result it was forced to undergo a restructuring, which resulted in deal execution problems and a subsequent slowdown in revenue for that region in the first quarter of FY 2020.

47. Defendants' revelation that the Americas segment was facing weaknesses, coupled with the drastic decline in license backlog, caused investor concern, as it evidenced reduced demand for the Company's products and ability to generate deals recognizable in future periods. Following the Company's May 30, 2019 disclosures, VMware's stock price declined over 7%.

48. Analysts were surprised by both the slowdown in the Americas segment and the sharp decline in license backlog following VMware's strong Q4 2019. The day following the Company's Q1 2020 earnings announcement, Deutsche Bank Research flagged the issues for investors, in an analyst report titled "First Signs of Macro Weakness," attributing the Company's practice of deferring historical sales to subsequent quarters for the sharp decline in license backlog to close out Q1 2020:

VMware said that the decision to realign/simplify US sales (new Sales leader, rep territory changes) was prompted by the Feb 2019 departure of America's head Brett Shirk (who joined Rubrik). ***We suspect that VMware's reluctance to raise its FY20 guide could also be driven by a desire to assess the impact of the sales changes. . . . The unbilled license backlog fell sharply to \$48m from \$147m in 4QF19, implying that a good portion of 1QF20 product billings were actually 4QF19 deals that got invoiced in 1QF20.***

49. In the following weeks, analysts continued to highlight the surprising depletion in license backlog. In a June 13, 2019 analyst report, Barclays highlighted that "***backlog is a helpful leading metric***" to understanding the Company's financial position, and that there was "***an investor debate around the depletion in license backlog*** (defined as unfulfilled POs relating to licenses and saw 40% sequential decline) for the quarter."

1 50. Shortly thereafter, Deutsche Bank Research issued another report again highlighting
2 the reduction in backlog. In its June 20, 2019 report, Deutsche Bank confirmed its previous report
3 regarding the Company's realignment in its Americas segment "*caused some unexpected*
4 *disruption,*" and "*deals were impacted.*" The Company spent the next several months "rebuilding
5 [the] momentum in the Americas," that was lost in Q1 2020.

6 51. The bad news continued. On August 22, 2019 (Q2 2020), the Company announced
7 another substantial decrease in its backlog – this time revealing that the Company's *total* backlog
8 plummeted 74% from a Class Period high of \$449 million at the end of FY 2019 just six months
9 prior, to \$117 million at the close of Q2 2020 – a decline of 35% from the prior quarter. Likewise,
10 the Company announced another large drop in its license backlog – a 73% decline from the previous
11 quarter, and a 91% decline over the course of six months – to end with just \$13 million, signaling
12 weakened demand for the Company's license products.

13 52. The same day, defendants also announced they were *decreasing* the Company's
14 license revenue guidance for the second half of FY 2020. Though defendants repeatedly assured
15 investors during the Class Period that the Company was successfully managing the industry-shift to
16 subscription and SaaS products, defendants attributed the lowered full FY 2020 guidance to
17 precisely that, the incremental mix shift toward subscription and SaaS. The shift to subscription and
18 SaaS product offerings negatively impacted the revenue the Company would recognize, as it was
19 ratably recognized over the subscription term, as opposed to license revenue that was recognized
20 more swiftly. Following VMware's August 22, 2019 disclosures, the Company's stock price again
21 dropped, falling from \$148 per share to \$133 per share – a decline of 10% – in one trading day.

22 53. Undeterred by the headwind the Company was facing on the timing of revenue
23 recognition in the subscription and SaaS product offerings, defendants continued to tout the strength
24 of its bookings pipeline heading into Q4 2020. During the earnings conference call for analysts and
25 investors on November 26, 2019 following the close of Q3 2020, defendants assured the market that
26 it remained "comfortable" with the balance of its revenue mix, and increased both FY 2020 total
27 revenue and license revenue guidance.

54. The same day, however, defendants announced yet another significant reduction in the Company's total backlog – a drop of another 39% from Q2 2020, to end the quarter at just \$71 million. In just nine months, VMware's total backlog fell over 84%. Yet again, the Company's revelations of declining backlog caused VMware's stock price to fall, this time nearly 6% in the two trading days following the Company's announcement.

F. Defendants Disclose that Backlog Has Virtually Disappeared and that VMware's Accounting for Backlog Is Being Investigated by the SEC

55. On February 27, 2020, one year after VMware posted record-breaking backlog, defendants disclosed that *despite* the substantial backlog it had entering FY 2020, VMware was unable to meet license and total revenue guidance for Q4 2020 and FY 2020. The Company also revealed that total backlog had declined to only \$18 million, which included just \$5 million in license backlog – a staggering decline of 96% and 97% for total and license backlog, respectively, from Q4 2019. As explained by defendant Rowe, the Company's backlog was a driver for the disappointing results as “in Q4 last year, we had . . . strong backlog that we were able to utilize.” Defendant Rowe added that we were “disappointed in our ability to execute” at the end of the quarter.

56. In a Form 8-K filed with the SEC the same day, the Company also revealed it was subject to an ongoing SEC investigation into the Company's backlog of unfilled orders. Specifically, the Form 8-K advised investors that, “[i]n December 2019, the staff of the Enforcement Division of the [SEC] requested documents and information related to VMware's backlog and associated accounting and disclosures.” The Form 8-K also advised investors that, although “VMware is fully cooperating with the SEC's investigation,” it was “unable to predict the outcome of this matter at this time.”

57. After regularly remarking over the course of the prior six quarters that the Company was weathering the industry shift away from license products in favor of subscription and SaaS products, defendants also finally revealed that the Company was in fact *not* managing the shift from license to subscription and SaaS revenue well. Defendants also disclosed that VMware failed to meet its license revenue growth targets for both Q4 2020 and FY 2020, and missed the Q4 2020

license revenue guidance defendants issued just three months prior by 5%. During the earnings conference call on February 27, 2020, defendant Gelsinger also revealed “revenue came in a bit short of expectations due to a higher mix of subscription and SaaS.”

58. The revenue shift toward subscription and SaaS products resulted in VMware reclassifying its revenue line items to specifically include subscription and SaaS as an individual line item, along with license and services. This reclassification was necessary so that the Company’s financial statements would finally reflect the nature of VMware’s revenue streams as the industry shifted away from a license model, which was becoming obsolete, in favor of the subscription and SaaS model. Defendants further revealed that they “expect on-premises license revenue to fluctuate more on a quarter-by-quarter basis than what we’ve seen previously. This is driven by a higher percent of subscription and SaaS being sold as well as the variability of large deals between quarters that have historically had a large license revenue impact.”

59. The Company’s stock price plummeted on the news, closing at a 52-week low of \$120.52 per share the next day – a one-day decline of over 11% – and a startling decline of over 41% from the Class Period high reached during Q1 2020.

60. Analysts were concerned about the decline in backlog and resultant SEC investigation. In a March 5, 2020 analyst report Deutsche Bank reported:

The SEC Request and VMware’s Backlog

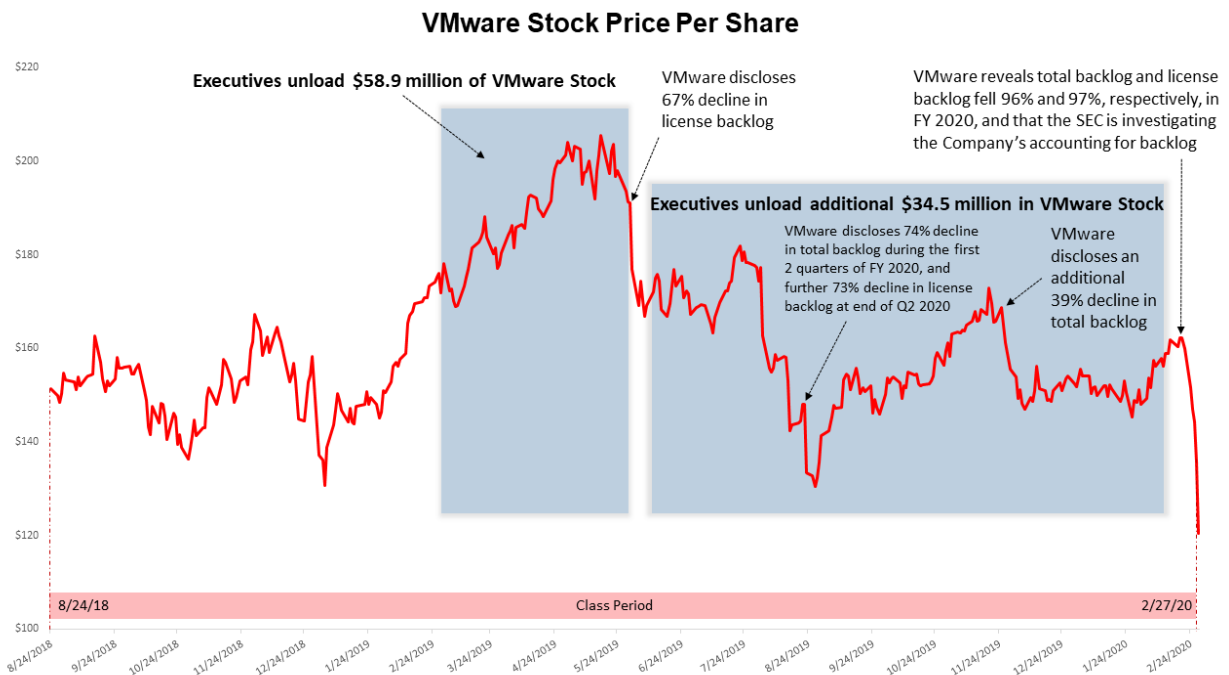
On the night of its earnings release last week, VMware also disclosed that the SEC “requested documents and information related to VMware’s backlog and associated accounting and disclosures.” VMware did not disclose any additional information but this has generated a few (not a ton of) questions from investors since the print. We believe that the document request related to VMware’s “unbilled backlog” disclosure, not to more critical and conventional backlog numbers like RPO or DR. *In 4QF20, VMware’s “unbilled backlog” metric (different than the gap between DR and RPO) of \$18 million was down massively from \$449 million in the year-ago quarter. VMware refers to this as a measure of “extended pipeline,” essentially signed or completed deals that have not yet been fulfilled or billed. Frankly, we’re unsure what to make of this metric as it only represents a fraction of VMware’s pipeline, but needless to say the steep y/y decline doesn’t make us feel great. Evidently the SEC has questions too.*

61. Throughout the Class Period, defendants touted the Company’s strong financial performance and repeatedly affirmed broad-based strength and growth across its product portfolio in each of its three geographic segments, while utilizing deliberately inflated backlog numbers to

conceal the truth that VMware's financial metrics were the product of an unsustainable license bookings revenue model that was becoming obsolete in the industry, and that the Company was plagued by decreased customer demand and execution problems, and weaknesses in its Americas segment.

62. While Lead Plaintiff and other members of the Class (as defined below) who purchased VMware shares at inflated prices have suffered hundreds of millions of dollars in harm as the truth entered the market, Company executives were able to unload over \$93 million of their own VMware stock at inflated prices in FY 2020 as illustrated in the figure below.

Figure 2:



V. DEFENDANTS' FALSE AND MISLEADING STATEMENTS DURING THE CLASS PERIOD

63. After the market closed on August 23, 2018, defendants held the Company's Q2 2019 earnings call for investors and analysts. During the earnings call, defendant Rowe remarked that the Company "exited Q2 [2019] with \$141 million of license backlog compared with \$122 million at the end of Q1."

64. During the question and answer segment on the earnings call, defendant Gelsinger explained that VMware was experiencing a “strong cycle” that would carry the Company through the long-term and “well into the future”:

And I would just say, as I said in my formal comments, Mark, that we believe we are in a strong cycle. Customers are resonating with the VMware strategy. ***Our execution is good and the market for technology is strong. And those are not this quarter statements. Those are long-term statements where we think that the business performance, our growth rates, the ability of customers to invest in the strategic product portfolio that we have. These are long-term trends and we believe that we’re in a very good cycle for the business for not just this quarter, but well into the future.***

65. On September 11, 2018, VMware filed with the SEC its quarterly report on Form 10-Q providing the Company’s financial and operating results for Q2 2019. Defendants Gelsinger and Rowe certified that the financial information in the 10-Q fairly represented, in all material respects, the financial condition and results of VMware’s operations, and that the report “does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made . . . not misleading.”

66. The Form 10-Q also stated that VMware’s “total backlog was \$320 million, generally consisting of licenses, maintenance and services. Our backlog related to licenses was \$141 million, which [it] generally expect[s] to deliver and recognize as revenue during the following quarter.”

67. Unbeknownst to analysts and investors, defendants knew or recklessly disregarded that the statements set forth in ¶¶63-66 above were each false and misleading or omitted material information necessary to make the statements not misleading, when made. The true facts, which were then known to, or recklessly disregarded by, the defendants based upon their access to and review of internal Company information, were:

(a) Defendants had misleadingly inflated license and total backlog by deferring current period sales to subsequent quarters; and

(b) The Company was experiencing an adverse shift toward subscription and SaaS product offerings, and its license model was becoming obsolete, impacting the rate at which VMware was able to recognize revenue.

68. After the market closed on November 29, 2018, the Company held its Q3 2019 earnings call with analysts and investors. During that call, defendant Rowe highlighted the strength of the Company's license backlog, informing analysts and investors that VMware "exited Q3 with \$144 million of license backlog compared with \$141 million at the end of Q2 [2019]. . . . As we've mentioned, license backlog is the license portion of unfulfilled orders at quarter end."

69. During the call, defendant Rowe also provided insight into FY 2020, stating "[w]e expect the strength we're seeing in the business to continue next year and are currently planning on total revenue growth of approximately 12% for FY '20, which includes accelerating our growth in hybrid cloud subscription and SaaS." Rowe continued, stating that the Company's increased guidance for FY 2020, and positive outlook for FY 2020 "*reflect the strength we continue to see in the business.*"

70. During the question and answer segment of the earnings call, defendant Rowe responded to an analyst question, explaining that defendants were comfortable with the Company's revenue mix between license bookings and subscription and SaaS bookings, and felt "very confident heading into [FY 2020]":

So we're very comfortable – if you take it all in aggregate, we're comfortable with that mix. *We're comfortable with the SaaS mix and the hybrid cloud mix that we're growing here at VMware. It's obviously highlighted in the guide for Q4 as well as in the guide for FY '20. So nothing there I would call out other than the fact that the business is performing well and we feel very confident heading into the next year.*

71. An analyst from Deutsche Bank described that the Company's preliminary FY 2020 revenue growth of 12%, was "appreciably above" the growth that analyst was modeling, and questioned whether "there [are] any other variables that might explain that good number that you'd care to highlight?"

72. Defendant Gelsinger responded:

Great. Thank you, Karl. *Sounds like you need to update your model.* So we're well underway in planning for next year, Karl. And with that, we're building detailed models for – across all the product lines, business investments, et cetera. And as indicated, we felt it was the appropriate time to get some direction for where we expect to land next year. Overall, we're not expecting anything, I'll say, dramatic, right, with the economic view. We continue to believe that technology is well positioned in the broader economic, so we expect that we're well outgrowing the overall economy as tech spend has the last couple of years and as I've described

1 it as tech breaking out of tech and what I've described as a superpower, mobility,
 2 cloud, IoT and AI, that these continue to be powerful trends that make technology
 3 more important in more areas of the business. But it isn't just those broader views.
 4 ***It really is that we're supporting that by the detailed planning that we're well***
 5 ***underway with as we build our plan for next year and the product opportunities.***
 6 And Zane will describe a little bit more in the pieces inside of that as you're calling
 7 out, in particular with some of these new areas of revenue, hybrid cloud, SaaS
 8 opportunities, the new acquisitions contributing to that as well.

9 73. Defendant Rowe added, "[w]e're very pleased with the growth, as you all know, with
 10 all of the emerging parts of the portfolio that we would expect to see continued growth in next year."

11 74. In closing, defendant Gelsinger reiterated that the Company was continuing its strong
 12 performance, highlighting the strength the Company expected in FY 2020:

13 Q3 was another strong quarter for us. We continue to be very pleased with the strong
 14 performance, our strategy, solutions as they resonate with customers. ***We also***
 15 ***pleased to give you our preliminary outlook on fiscal 2020, and it really reflects the***
 16 ***strength we continue to see in the business and our strategy.***

17 75. On December 10, 2018, VMware filed with the SEC its quarterly report on Form 10-
 18 Q providing the Company's financial and operating results for Q3 2019. Defendants Gelsinger and
 19 Rowe certified that the financial information in the Form 10-Q fairly represented, in all material
 20 respects, the financial condition and results of VMware's operations, and that the report "does not
 21 contain any untrue statement of a material fact or omit to state a material fact necessary to make the
 22 statements made . . . not misleading."

23 76. The Form 10-Q stated that VMware's "total backlog was \$324 million." Of that total,
 24 the "backlog related to licenses was \$144 million, which [the Company] generally expect[s] to
 25 deliver and recognize as revenue during the following quarter."

26 77. Unbeknownst to analysts and investors, defendants knew or recklessly disregarded
 27 that the statements set forth in ¶¶68-76 above were each false and misleading or omitted material
 28 information necessary to make the statements not misleading, when made. The true facts, which
 were then known to, or recklessly disregarded by, the defendants based upon their access to and
 review of internal Company information, were:

(a) Defendants had misleadingly inflated license and total backlog by deferring
 current period sales to subsequent quarters; and

(b) The Company was experiencing an adverse shift toward subscription and SaaS product offerings, and its license model was becoming obsolete, impacting the rate at which VMware was able to recognize revenue.

78. On February 28, 2019, VMware filed with the SEC a Form 8-K attaching a press release announcing the Company's results of operations for the quarter and fiscal year ended February 1, 2019 (Q4 2019). In the press release, remarking on behalf of the Company, defendant Gelsinger stated "Q4 was a terrific ending to a strong fiscal '19 driven by broad-based strength across our diverse product portfolio *and in all three geographies.*"

79. The same day, the Company held an earnings conference call for investors and analysts. During that call, Gelsinger touted that "*Q4 was a terrific ending to a strong fiscal '19,*" with double-digit revenue growth "driven by broad-based strength across our diverse product portfolio *and in all 3 geographies.*"

80. Commenting on the strength of the Company's license backlog, Rowe stated that VMware "exited Q4 with \$147 million of license backlog compared to \$144 million at the end of Q3." Following the strong license growth to end FY 2019, the Company upwardly revised FY 2020 guidance.

81. Analysts were curious how VMware was experiencing continued revenue growth while other major tech companies were experiencing slowdowns. During the earnings call, one analyst at Deutsche Bank highlighted his concern about potential downturns in the industry:

It felt to me like in 2018, that every single tech supplier exposed to infrastructure IT had a terrific year, but in the last month-or-so, we've seen weakness from Intel, NVIDIA, NetApp, HP, and now Nutanix tonight, and *yet you just posted one of your strongest revenue growth quarters in years. And I'm wondering if you could just explain that apparent divergence.* Is it a function of the emerging products becoming a larger portion of the mix? Is it enterprise demand maybe transitioning from hardware to more software defined? Your thoughts will be welcome."

82. In response to the analyst's concerns, defendant Gelsinger reassured investors that VMware was "extremely" well-positioned to navigate the turbulent IT market as a tech "winner[]":

Thanks, Karl, and yes, we are very happy with the quarter's performance. And we do continue to see that it will be a good IT market into the future overall. And as you've heard me talk about in the past, I see it as sort of tech breaking out of tech. More areas consuming technology, more areas of every business differentiating and it's no longer IT is buying technology, it's now every aspect of the business. So

overall, we continue to see a good tech market. Now inside of that, hey, I think there's some turbulence. There's going to be winners and losers. We continue to see lots of questions on cloud, private and public cloud, and how hybrid cloud transitions. You're clearly going to see these normal cycles of over and undersupply as people are building up rapidly in different geos. Clearly, there is a whole lot of those other effects that are going to play out where I think we're going to see some winners and losers. *When we look at that against our business, we've just positioned ourselves, we believe, extremely well in many of these growth sectors. And we're no longer dependent on any geo or any individual product, but the real breadth of our portfolio is nicely rewarding us across the broad landscape of, we believe a good tech market that's going to continue well into the future. And there will be winners and losers inside of that because there is so much change going on in the marketplace with these powerful trends. You might remember, I've talked about the 4 superpowers: cloud, mobility, AI and Edge and IoT, and all of those will have different effects of who's going to be the winners and losers inside of it. But it's a good market and really happy with our performance.* Thank you, Karl.

83. On March 29, 2019, VMware filed with the SEC its annual report on Form 10-K providing the Company's financial and operating results for the fiscal year ended February 1, 2019. Defendant Gelsinger signed the FY 2019 Form 10-K and defendants Gelsinger and Rowe certified that the financial information in the 10-K represented, in all material respects, the financial condition and results of VMware's operations, and that the report "does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made . . . not misleading."

84. The Form 10-K stated that license revenue "continued to benefit from broad-based growth across our diverse product portfolio and across our U.S. and international geographies."

85. The Form 10-K also stated that "As of February 1, 2019, our total backlog was approximately \$449 million. Backlog primarily consists of licenses, maintenance and services. Our backlog related to licenses was approximately \$147 million, which we generally expect to deliver and recognize as revenue during the following quarter."

86. Unbeknownst to analysts and investors, defendants knew or recklessly disregarded that the statements set forth in ¶¶78-85 above were each false and misleading or omitted material information necessary to make the statements not misleading, when made. The true facts, which were then known to, or recklessly disregarded by, the defendants based upon their access to and review of internal Company information, were:

1 (a) Defendants had misleadingly inflated license and total backlog by deferring
2 current period sales to subsequent quarters;

3 (b) The Company was experiencing an adverse shift toward subscription and
4 SaaS product offerings, and its license model was becoming obsolete, impacting the rate at which
5 VMware was able to recognize revenue; and

6 (c) The Company was experiencing turmoil in its Americas region following the
7 departure of its segment leader just weeks prior, resulting in a restructuring in that region, which
8 compromised VMware's ability to execute deals and recognize revenue in that region.

9 87. On May 30, 2019, VMware filed with the SEC a Form 8-K attaching a press release
10 announcing the Company's results of operations for the quarter ended May 3, 2019 (Q1 2020). The
11 press release disclosed "[t]otal revenue growth of 13% year-over-year," total "[r]evenue for the first
12 quarter was \$2.27 billion, an increase of 13% from the first quarter of fiscal 2019," and "[l]icense
13 revenue for the first quarter was \$869 million, an increase of 12% from the first quarter of fiscal
14 2019." According to the Company, "[t]otal revenue plus sequential change in total unearned
15 revenue grew 25% year-over-year," while "[l]icense revenue plus sequential change in unearned
16 license revenue grew 23% year-over-year."

17 88. In the press release, remarking on behalf of the Company, defendant Gelsinger stated
18 ***"Q1 was a good start to fiscal 2020 with strength across our comprehensive solutions portfolio."***

19 89. After market hours the same day, the Company held an earnings conference call for
20 investors and analysts. During that call, defendant Gelsinger stated that the Company's "revenue for
21 the quarter increased 13% year-over-year," and remarked that the Company was ***"very well
22 positioned to execute on our plans for the full year."***

23 90. Also during the earnings call, defendant Rowe reiterated that "[i]n Q1, total revenue
24 grew 13% and license revenue increased 12% year-over-year," and detailed that the Company's
25 "[g]rowth in revenue, plus the sequential change in unearned revenue for the quarter, was 25% or up
26 20% when excluding an ASC 606 reclassification adjustment, which reduced unearned revenue in
27 Q1 of fiscal '19." At the same time, defendant Rowe stated, "[l]icense revenue, plus the sequential
28

1 change in unearned license revenue, grew 23% year-over-year or up 17%, excluding the same 606
2 reclassification adjustment in Q1 of '19."

3 91. During the earnings call, defendant Rowe also informed investors that the Company's
4 license backlog fell drastically from the prior quarter, stating "[w]e exited Q1 with \$48 million of
5 license backlog compared to \$147 million at the end of Q4 FY '19." Rowe confirmed that Q1 2020
6 was a ***"Q1 was a good start to FY '20, and we're maintaining our positive outlook for the year,"***
7 including full-year "total revenue growth of 11.8% year-over-year to \$10.030 billion. . . . [and]
8 [l]icense revenue growth of 12.8% to \$4.275 billion." Defendant Rowe stated that "[f]or Q2 FY '20,
9 total revenue is expected to be \$2.425 billion, up 11.5% year-over-year with license revenue of \$1
10 billion, an increase of 11.1% year-over-year." The Company's performance during Q1 2020,
11 defendant Rowe stated, ***"has us well positioned to execute on our plans for the year."***

12 92. For the second quarter in a row, analysts questioned how VMware was able to
13 maintain such strong guidance when other infrastructure software companies had "soft quarter[s],"
14 with a Jefferies LLC analyst asking how VMware was unaffected by the downturn in the market:

15 And I don't want to spend too much time on that because it was really strong results
16 here. But VMware side, I guess, Pat and Zane, too, if you have anything to
17 contribute here, you have a view that we don't have, right? Like why do you think
so many others are seeing some softness out there? Because they are. I mean, I got 3
companies tonight and you guys are a lot better than the other 2. I don't know.

18 Is it – are there hardware issues out there? Like, with tariffs and other things,
19 which has now trickled to infrastructure software and then apps? But that seems too
20 early for something like that to happen. Do you have anything you can share with us
here? And also, why hasn't this really affected you?

21 93. Again, defendant Gelsinger alluded that VMware was a "winner[]" in the tech
22 market, which lead to the solid quarter:

23 Thanks, John, for the comments. We do think that some of the
24 macroeconomic effects, that will affect everybody, right, in that environment. ***As
you've heard me say before, there's going to be some winners and losers on
different technology trends inside of that.***

25 Overall, we continue to be optimistic. We continue to be optimistic on the
26 long-term view of the market, that IT growth is going to outpace GDP growth,
27 enterprise as a software growth will outpace IT growth. We see this sort of tech
breaking out of tech and more businesses, right, being – becoming centered on their
technology differentiation.

1 Clearly, some of the trade aspects, some of the different cyclicalities going on
affects different players. But overall, we remain optimistic. ***Our strategy is***
2 ***resonating well into the future and super pleased with the execution of my team to***
3 ***deliver a very solid quarter.***

4 94. Defendant Rowe echoed defendant Gelsinger's comments, citing the Company's
5 "consistency" in the face of market volatility and uncertainty:

6 John, I would just add to Pat's point. We're not immune to it. We feel good
about the start of the year, as you pointed out, and we feel like we've had some
7 consistency as we thought about the year and it's playing out to some degree and to
some extent as we expected.

8 I'll also point out the customer ROI for their investment in our product
portfolio is strong. So I think that resonates. I think the strategy resonates and we're
9 benefiting from that. I think some of what you're seeing across the broader
landscape is some volatility and obviously uncertainty tied to the macroeconomic
10 environment. ***But beyond that, we're comfortable with what we're seeing early and***
feel good about our forecast for the year.

11 95. In response to another analyst's question, defendant Gelsinger stated he felt
12 "comfortable" maintaining guidance for the first half of the year, but indicated the Company
13 expected to see momentum heading into the second half of FY 2020:

14 We are seeing strong execution by our teams that's continuing to give us
15 strength. We think our strategy is well positioned for it. But it's still early in the
year. We've got a lot of year to go execute yet with some of those uncertainties
16 around us. ***And we're feeling quite good about the momentum that we see going***
into Q2 and for the second half.

17 96. Defendant Rowe reiterated that defendants remained "comfortable with how
18 [VMware is] positioned for the year," despite "some of our competitors seeing a little bit of
19 weakness and some volatility and variability quarter-to-quarter."

20 97. On June 10, 2019, VMware filed with the SEC its quarterly report on Form 10-Q
21 providing the Company's financial and operating results for the quarter ended May 3, 2019. In the
22 Form 10-Q, the Company reported Q1 2020 total revenue of \$2.266 billion, and license revenue of
23 \$869 million for the quarter.

24 98. Defendants Gelsinger and Rowe certified that the financial information in the Form
25 10-Q fairly represented, in all material respects, the financial condition and results of VMware's
26 operations, and that the report "does not contain any untrue statement of a material fact or omit to
27 state a material fact necessary to make the statements made . . . not misleading."
28

1 99. The Form 10-Q stated that license revenue “continued to benefit from broad-based
2 growth across our diverse product portfolio and across our U.S. and international geographies.”

3 100. The Form 10-Q also stated that “As of May 3, 2019, our total backlog was \$180
4 million. Backlog primarily consists of licenses, maintenance and services. Our backlog related to
5 licenses was \$48 million, which we generally expect to deliver and recognize as revenue during the
6 following quarter.”

7 101. Unbeknownst to analysts and investors, defendants knew or recklessly disregarded
8 that the statements set forth in ¶¶87-100 above were each false and misleading or omitted material
9 information necessary to make the statements not misleading, when made. The true facts, which
10 were then known to, or recklessly disregarded by, the defendants based upon their access to and
11 review of internal Company information, were:

12 (a) Defendants had misleadingly inflated license and total backlog by deferring
13 current period sales to subsequent quarters;

14 (b) Had VMware recognized the revenue that was deferred into backlog during
15 FY 2019 when it was in fact secured, VMware would have delivered only low single digit revenue
16 growth for FY 2020;

17 (c) The Company was experiencing an adverse shift toward subscription and
18 SaaS product offerings, and its license model was becoming obsolete, impacting the rate at which
19 VMware was able to recognize revenue;

20 (d) The Company was not well positioned to execute for the year, because
21 VMware lacked the ability to properly execute its pipeline and suffered from deal timing issues that
22 negatively affected the Company’s ability to meet revenue guidance; and

23 (e) Reported revenue was misleading as it included revenue from sales that were
24 secured in, and should have been recognized in, FY 2019.

25 102. On August 22, 2019, VMware filed with the SEC a Form 8-K attaching a press
26 release announcing the Company’s results of operations for the quarter ended August 2, 2019 (Q2
27 2020). In the press release, the Company announced “Strong Q2 performance; Total revenue growth
28 of 12% year-over-year,” with total “[r]evenue for the second quarter [of] \$2.44 billion, an increase of

1 12% from the second quarter of fiscal 2019,” and “[l]icense revenue for the second quarter [of]
2 \$1.01 billion, an increase of 12% from the second quarter of fiscal 2019.” The press release revealed
3 total revenue of \$2.439 billion, and license revenue of \$1.011 billion, and that “[t]otal revenue plus
4 sequential change in total unearned revenue grew 17% year-over-year,” while “[l]icense revenue
5 plus sequential change in unearned license revenue grew 12% year-over-year.”

6 103. Remarking on behalf of the Company, defendant Gelsinger stated the Company was
7 “[b]uilding on another solid quarter,” and defendant Rowe stated “[w]e are pleased with our
8 strong financial performance in Q2, which reflected broad-based strength in all three geographies.”

9 104. After market hours the same day, the Company held an earnings conference call for
10 investors and analysts, during which defendant Gelsinger reiterated “[t]otal revenue for the quarter
11 increased 12% year-over-year,” with defendant Rowe echoing “[w]e’re pleased with our
12 performance in Q2. We reported 12% year-over-year growth in total revenue and license revenue
13 driven by strength across our broad products and solutions portfolio in all 3 geographies.”

14 105. For the second quarter in a row, the Company reported a dramatic shift in license
15 backlog. During the conference call, defendant Rowe reported that, at the end of Q2 2020, the
16 Company “had license backlog of \$13 million and total backlog of \$117 million.”

17 106. During the earnings call, defendant Rowe informed investors and analysts that
18 “[w]e’re forecasting growth in total revenue plus the sequential change in total unearned revenue to
19 be approximately 13% year-over-year in the quarter and up about 2 percentage points versus Q3 FY
20 ‘19.”

21 107. During the earnings call, a Citigroup Inc. analyst asked whether the progression to
22 subscription and SaaS products would “suppress license growth.” In response, defendant Rowe
23 confirmed that he believed the Company “can grow both the perpetual [license] side of the business
24 as well as grow the SaaS side.”

25 108. On September 9, 2019, VMware filed with the SEC its quarterly report on Form 10-Q
26 providing the Company’s financial and operating results for the quarter ended August 2, 2019. In
27 the Form 10-Q, the Company disclosed total revenue of \$2.439 billion, of which \$1.011 billion was
28 license revenue. Defendants Gelsinger and Rowe certified that the financial information in the Form

1 10-Q fairly represented, in all material respects, the financial condition and results of VMware's
2 operations, and that the report "does not contain any untrue statement of a material fact or omit to
3 state a material fact necessary to make the statements made . . . not misleading."

4 109. The Form 10-Q again stated that license revenue "continued to benefit from broad-
5 based growth across our diverse product portfolio and across our U.S. and international
6 geographies."

7 110. The Form 10-Q also stated that "[a]s of August 2, 2019, our total backlog was \$117
8 million. Backlog primarily consists of licenses, maintenance and services. Our backlog related to
9 licenses was \$13 million, which we generally expect to deliver and recognize as revenue during the
10 following quarter."

11 111. Unbeknownst to analysts and investors, defendants knew or recklessly disregarded
12 that the statements set forth in ¶¶102-110 above were each false and misleading or omitted material
13 information necessary to make the statements not misleading, when made. The true facts, which
14 were then known to, or recklessly disregarded by, the defendants based upon their access to and
15 review of internal Company information, were:

16 (a) Defendants had misleadingly inflated license and total backlog by deferring
17 current period sales to subsequent quarters;

18 (b) Had VMware recognized the revenue that was deferred into backlog during
19 FY 2019 when it was in fact secured, VMware would have delivered only low single digit revenue
20 growth for FY 2020;

21 (c) The Company was experiencing an adverse shift toward subscription and
22 SaaS product offerings, and its license model was becoming obsolete, impacting the rate at which
23 VMware was able to recognize revenue;

24 (d) The Company was not well positioned to execute for the year, because
25 VMware lacked the ability to properly execute its pipeline and suffered from deal timing issues that
26 negatively affected the Company's ability to meet revenue guidance; and

27 (e) Reported revenue was misleading as it included revenue from sales that were
28 secured in, and should have been recognized in, FY 2019.

1 112. On November 26, 2019, VMware filed with the SEC a Form 8-K attaching a press
2 release announcing the Company's results of operations for the quarter ended November 1, 2019 (Q3
3 2020). In the press release, the Company disclosed "[t]otal revenue growth of 12% year-over-year,"
4 with "[r]evenue for the third quarter [of] \$2.46 billion, an increase of 12% from the third quarter of
5 fiscal 2019," and "[l]icense revenue for the third quarter [of] \$974 million, an increase of 10% from
6 the third quarter of fiscal 2019."

7 113. The press release disclosed that "[t]otal revenue plus sequential change in total
8 unearned revenue grew 18% year-over-year," or 12% year-over-year excluding the excluding the
9 unearned revenue assumed by the Company with its acquisition of Carbon Black, while at the same
10 time, "[l]icense revenue plus sequential change in unearned license revenue grew 21% year-over-
11 year," or 13% excluding unearned revenue assumed during the acquisition.

12 114. In the press release, remarking on behalf of the Company, defendant Gelsinger stated
13 ***"Q3 was another solid quarter for VMware, and we're pleased with our results. We continue to***
14 ***see traction and customer momentum in support of VMware's vision to deliver a software***
15 ***architecture that enables any app, on any cloud, delivered to any device."*** Defendant Rowe echoed
16 that sentiment, stating ***"[w]e're pleased with our financial performance and execution this***
17 ***quarter, which reflected broad-based strength across our product and solutions portfolio."***

18 115. After market hours the same day, the Company held an earnings conference call for
19 investors and analysts. During that call, Defendant Gelsinger remarked that "Q3 was another solid
20 quarter for VMware, and we're pleased with our results. We continue to see traction and customer
21 momentum in support of VMware's vision to deliver a software architecture that enables any app, on
22 any cloud, delivered to any device." Defendant Gelsinger disclosed "[i]n Q3, total revenue increased
23 12% year-over-year."

24 116. Defendant Rowe again touted the Company's performance, stating "[w]e're pleased
25 with our financial performance and execution this quarter, which resulted in total revenue growth of
26 12% and license revenue growth of 10% year-over-year."

117. For the third quarter in a row, defendant Rowe announced a significant reduction in the Company's license backlog, stating "[a]t quarter end, we had license backlog of \$33 million and total backlog of \$71 million."

118. As a result of the Company's Q3 2020 performance, defendants increased guidance for the full-year FY 2020. Defendant Rowe disclosed, "[f]or the full year, we are projecting an increase in total revenue to \$10,100,000,000, up 12.5% year-over-year. This includes the addition of Carbon Black's financials post close, which accounts for the largest portion of the revenue increase. We expect license revenue of \$4,245,000,000 for FY '20, up 12% year-over-year." As for the final quarter of FY 2020, defendant Rowe stated, "[m]oving to our Q4 guidance. License revenue is expected to be \$1,390,000,000, an increase of 13% year-over-year, and total revenue is expected to be \$2,950,000,000, up 13.8% year-over-year."

119. During the question and answer session of the earnings call, defendant Rowe reiterated that the Company saw strength in Q3 2020, and expected that strength to continue with a solid pipeline of bookings heading into Q4 2020, which was reflected in the Company's Remaining Performance Obligations ("RPO") line item, within which license backlog was included:

As you point out, we saw really good booking strength in the quarter. And we have a solid guide for the rest of the year. I talked about RPO, which, for the third quarter, was \$8.5 billion, which has also grown nicely year-over-year, *reflecting the ongoing strength of the business. So yes, we feel good about the guide. We feel good about our pipeline heading into Q4.*

120. Responding to a separate analyst question about the Company's revenue guidance for Q4 2020 and FY 2021, defendant Rowe again reiterated that VMware's revenue guidance was driven by the Company's pipeline heading into Q4 2020:

But again, if you recall, the guide also highlighted some of the growth that we're anticipating for the second half of the year based on what we said last quarter. *So we feel really good about the pipeline heading into the fourth quarter and the solid guide for the year.*

121. The revenue mix shift from licenses to subscription and SaaS was important to analysts. When specifically asked by a Mizuho Securities USA LLC analyst whether the Company anticipated a "headwind on revenue growth" due to the slower revenue recognition stream of

1 subscription and SaaS. Defendant Rowe assured the analysts and investors that the Company
2 “feel[s] good about the trajectory heading into next year,”

3 Yes. It’s a great question. I’m not sure it’s as good as Pat’s. But as we
4 called out, as we called out in the third quarter, it was more pronounced on the
5 license revenue side, and what we’ve generally done is steered you more towards
6 total revenue and with the strength we’ve seen in the third quarter, candidly, in both
7 categories. I mean as you know, hybrid cloud subscription and SaaS, while we get
8 the bookings now, we recognize the revenue over an extended period of time. And
9 that’s sort of the nuance when you’re thinking about the balance between license
10 revenue versus hybrid cloud subscription SaaS. That’s sort of the balance that we
11 were contemplating in the third quarter. And we mentioned, with that strength, we
12 saw the guide continue through the year.

13 So there’s always a little bit of headwind, especially as you’re growing that
14 just because you essentially recognize the revenue slightly differently. We wouldn’t
15 call it out specifically as far as a percent because I think all of our – when we think
16 about those businesses, they’re all in different points on the maturity curve. ***But in***
17 ***aggregate, you’re right, there’s always that balance when you’re considering a***
18 ***perpetual model versus the SaaS model, but we’re comfortable with that balance.***
19 ***We’ve maintained the annual guide. We feel good about the trajectory heading***
20 ***into next year.***

21 122. On December 6, 2019, VMware filed with the SEC its quarterly report on Form 10-Q
22 providing the Company’s financial and operating results for the quarter ended November 1, 2019. In
23 the Form 10-Q the Company disclosed total revenue of \$2.456 billion, and license revenue of \$974
24 million. Defendants Gelsinger and Rowe certified that the financial information in the Form 10-Q
25 fairly represented, in all material respects, the financial condition and results of VMware’s
26 operations, and that the report “does not contain any untrue statement of a material fact or omit to
state a material fact necessary to make the statements made . . . not misleading.”

27 123. The Form 10-Q again stated that license revenue “continued to benefit from broad-
28 based growth across our diverse product portfolio and across our U.S. and international
geographies.”

124. The Form 10-Q also stated that “[a]s of November 1, 2019, our total backlog was \$71
million. Backlog primarily consists of licenses, maintenance and services. Our backlog related to
licenses was \$33 million, which we generally expect to deliver and recognize as revenue during the
following quarter.”

125. Unbeknownst to analysts and investors, defendants knew or recklessly disregarded
that the statements set forth in ¶¶112-124 above were each false and misleading or omitted material

1 information necessary to make the statements not misleading, when made. The true facts, which
 2 were then known to, or recklessly disregarded by, the defendants based upon their access to and
 3 review of internal Company information, were:

4 (a) Defendants had misleadingly inflated license and total backlog by deferring
 5 current period sales to subsequent quarters;

6 (b) Had VMware recognized the revenue that was deferred into backlog during
 7 FY 2019 when it was in fact secured, VMware would have delivered only low single digit revenue
 8 growth for FY 2020;

9 (c) The Company was experiencing an adverse shift toward subscription and
 10 SaaS product offerings, and its license model was becoming obsolete, impacting the rate at which
 11 VMware was able to recognize revenue;

12 (d) The Company was not well positioned to execute for the year, because
 13 VMware lacked the ability to properly execute its pipeline and suffered from deal timing issues that
 14 negatively affected the Company's ability to meet revenue guidance; and

15 (e) Reported revenue was misleading as it included revenue from sales that were
 16 secured in, and should have been recognized in, FY 2019.

17 **VI. ADDITIONAL SCIENTER AND MATERIALITY ALLEGATIONS**

18 126. During the Class Period, defendants were in possession of material nonpublic
 19 information concerning VMware's operations, finances, financial condition, and future business
 20 prospects, including, but not limited to, the true facts referenced above. Notwithstanding their duty
 21 to refrain from trading in VMware common stock, without disclosing the foregoing materially
 22 adverse nonpublic facts, the Individual Defendants and other VMware executives sold 702,270
 23 shares of VMware common stock during the Class Period at highly inflated prices, while in
 24 possession of material nonpublic information.

25 127. During the Class Period defendant Gelsinger sold \$23.4 million of VMware stock
 26 (over 141,000 shares) at inflated prices while in the possession of material non-public information.
 27 In contrast to his large Class Period stock sales, prior to the start of the Class Period, defendant
 28 Gelsinger sold *no* VMware stock in the 18 months directly preceding the Class Period. In fact,

despite the vesting of defendant Gelsinger's exercisable shares as early as 2014, defendant Gelsinger sold none of his VMware stock until September 2018, just after the start of the Class Period.

128. On March 1, 2019, the day after the Company disclosed record-breaking license backlog, defendant Gelsinger sold 21,086 shares of his VMware stock at prices as high as \$181.61 per share for proceeds of \$3.77 million.

129. During the Class Period, defendant Rowe sold 104,218 shares of VMware stock at inflated prices while in the possession of material nonpublic information to yield proceeds of \$17.8 million. Notably, in the 18 months preceding the Class Period, defendant Rowe made only two transactions, selling a total of only 13,100 shares for \$1.76 million in proceeds. In contrast, during the Class Period defendant Rowe sold 104,218 shares for proceeds of more than \$17.8 million, an increase of **915%**.

130. In total, VMware executives sold over 702,000 shares of stock during the Class Period at inflated prices for proceeds in excess of \$118.6 million. These sales are summarized in the following chart:

VMware.com (VMW) 08/24/2018 – 2/27/2020 Executive Sales Summary

Filer Name	Transaction Date	Price	Shares Sold	Proceeds
Carli Maurizio Executive Vice President, Worldwide Sales and Services	9/7/2018	\$152.54	3,779	\$ 576,449
	1/11/2019	\$147.58	1,989	\$ 293,537
	1/11/2019	\$146.74	34,859	\$ 5,115,210
	3/12/2019	\$174.25	5,446	\$ 948,966
	4/2/2019	\$182.63	14,000	\$ 2,556,820
	4/2/2019	\$183.60	13,647	\$ 2,505,589
	10/11/2019	\$156.37	26,899	\$ 4,206,197
	12/12/2019	\$154.20	2,075	\$ 319,965
Class Period Total:			102,694	\$ 16,522,731
Gelsinger (Patrick P) Chief Executive Officer	9/4/2018	\$152.61	11,804	\$ 1,801,408
	9/4/2018	\$150.69	1,602	\$ 241,405
	9/4/2018	\$151.84	11,594	\$ 1,760,433
	11/7/2018	\$150.00	25,000	\$ 3,750,000
	1/11/2019	\$146.64	18,058	\$ 2,648,025
	1/11/2019	\$147.37	9,437	\$ 1,390,731
	1/11/2019	\$145.56	2,600	\$ 378,456
	3/1/2019	\$180.51	1,965	\$ 354,702
	3/1/2019	\$179.51	4,792	\$ 860,212

1		3/1/2019	\$181.61	900	\$	163,449
2		3/1/2019	\$177.62	4,452	\$	790,764
3		3/1/2019	\$176.52	1,500	\$	264,780
4		3/1/2019	\$178.55	7,477	\$	1,335,018
5		5/1/2019	\$204.83	5,786	\$	1,185,146
6		5/1/2019	\$203.85	9,113	\$	1,857,685
7		5/1/2019	\$202.89	5,101	\$	1,034,942
8		7/19/2019	\$180.00	20,000	\$	3,600,000
9		Class Period Total:		141,181	\$	23,417,158
10	Kryslar (Patrick Kevan)	9/20/2018	\$152.28	4,984	\$	758,964
11	Chief Accounting Officer	4/3/2019	\$185.78	4,749	\$	882,269
12		4/3/2019	\$184.86	3,800	\$	702,468
13		4/4/2019	\$180.75	3,444	\$	622,503
14		6/11/2019	\$173.96	2,661	\$	462,908
15		9/10/2019	\$145.00	1,589	\$	230,405
16		Class Period Total:		21,227	\$	3,659,516
17	Olli Amy	9/20/2018	\$152.77	1,500	\$	229,155
18	Fliegelman	3/14/2019	\$178.98	1,723	\$	308,383
19	Senior Vice President, General Counsel	4/22/2019	\$189.32	100	\$	18,932
20		4/22/2019	\$188.69	1,400	\$	264,166
21		4/22/2019	\$187.58	957	\$	179,514
22		9/10/2019	\$150.00	2,753	\$	412,950
23		10/2/2019	\$151.62	1,228	\$	186,189
24		Class Period Total:		9,661	\$	1,599,289
25	Poonen Sanjay	1/8/2019	\$145.55	3,400	\$	494,870
26	Chief Operating Officer, Customer Operations	1/8/2019	\$146.27	5,056	\$	739,541
27		1/9/2019	\$149.98	7,679	\$	1,151,696
28		3/18/2019	\$182.60	50,000	\$	9,130,000
29		4/15/2019	\$191.97	30,000	\$	5,759,100
30		Class Period Total:		96,135	\$	17,275,208
31	Raghuram (Rangarajan)	3/11/2019	\$169.77	14,412	\$	2,446,725
32	Chief Operating Officer, Products & Cloud	3/11/2019	\$170.55	21,899	\$	3,734,874
33		4/1/2019	\$182.39	13,000	\$	2,371,070
34		4/1/2019	\$184.15	200	\$	36,830
35		4/1/2019	\$181.20	4,800	\$	869,760
36		4/1/2019	\$183.03	27,741	\$	5,077,435
37		9/3/2019	\$141.02	2,459	\$	346,768
38		9/3/2019	\$140.58	22,319	\$	3,137,605
39		10/2/2019	\$151.62	2,150	\$	325,983
40		11/4/2019	\$163.87	13,629	\$	2,233,384
41		11/4/2019	\$162.99	10,283	\$	1,676,026
42		11/4/2019	\$164.67	800	\$	131,736
43		Class Period Total:		133,692	\$	22,388,198

1	Ramaswami (Rajiv)	9/14/2018	\$160.00	6,000	\$	960,000
2	Chief Operating Officer, Products & Cloud	11/2/2018	\$142.92	3,575	\$	510,939
3		11/2/2018	\$144.64	3,670	\$	530,829
4		11/2/2018	\$143.65	5,100	\$	732,615
5		4/2/2019	\$184.68	4,430	\$	818,132
6		5/2/2019	\$200.34	1,800	\$	360,612
7		5/2/2019	\$199.05	1,902	\$	378,593
8		5/2/2019	\$198.46	4,068	\$	807,335
9		5/2/2019	\$202.19	3,665	\$	741,026
10		5/2/2019	\$201.41	3,427	\$	690,232
11		6/4/2019	\$171.63	4,773	\$	819,190
12		6/4/2019	\$170.85	18,533	\$	3,166,363
13		6/4/2019	\$169.93	15,507	\$	2,635,105
14		10/2/2019	\$151.62	2,150	\$	325,983
15		11/4/2019	\$163.22	8,238	\$	1,344,606
16		11/4/2019	\$163.99	6,424	\$	1,053,472
17		11/4/2019	\$164.73	200	\$	32,946
18	Class Period Total:			93,462	\$	15,907,979
19						
20	Rowe (Zane C)	12/12/2018	\$165.08	6,500	\$	1,073,020
21	Executive Vice President and Chief Financial Officer	4/2/2019	\$183.56	27,530	\$	5,053,407
22		4/2/2019	\$182.61	17,990	\$	3,285,154
23		4/2/2019	\$184.26	3,110	\$	573,049
24		6/13/2019	\$175.52	7,920	\$	1,390,118
25		6/13/2019	\$174.86	13,208	\$	2,309,551
26		6/13/2019	\$176.71	1,451	\$	256,406
27		9/5/2019	\$148.18	3,656	\$	541,746
28		9/5/2019	\$148.85	2,900	\$	431,665
29		9/5/2019	\$147.08	13,444	\$	1,977,344
30		12/6/2019	\$148.38	6,309	\$	936,129
31		12/6/2019	\$148.89	200	\$	29,778
32	Class Period Total:			104,218	\$	17,857,367
33						
34	Class Period Grand Total:			702,270	\$	118,627,445

131. The executives' Class Period sales were dramatically out of line with the executives' prior trading practices. During the 18 months prior to the Class Period (February 23, 2017 to August 23, 2018), VMware executives collectively sold only 251,867 shares of VMware stock, for proceeds

of under \$31.8 million.³ Thus the total number of shares sold, and proceeds received during the Class Period, by VMware's executives increased by 179% and 272%, respectively.

132. The executive sales were also suspicious in timing as they occurred at times calculated to maximize personal benefit from undisclosed inside information. As demonstrated above, VMware executives sold \$84.1 million in VMware stock between August 2018 and May 2019, at inflated prices as high as \$204.83 per share (just \$0.69 shy of VMware's all-time high), during the period that backlog was increased by deferring current period sales into future periods.

133. As illustrated in the chart above, from March 1, 2019 – the day immediately following the Company's FY 2019 positive earnings announcement of record-breaking backlog numbers – through May 2, 2019 – just *one day* prior to the close of Q1 2020 – VMware executives, including the Individual Defendants, unloaded \$58.9 *million* in VMware stock at inflated prices, as high as \$204.83 per share.⁴ Thus, *50%* of the executives' sales during the Class Period were made in the *3-month period* between the Company's announcement of all-time high license backlog on February 28, 2019, and the time the Company announced a drastic, 67% decline in license backlog on May 30, 2019. Indeed, defendant Gelsinger alone sold 20,000 shares on May 1, 2019, just two days before the close of Q1 2020, at prices near the Company's all-time high, for proceeds of approximately \$4 million.

134. The executives' suspicious trading continued throughout the Class Period, as defendants and other executives took advantage of the artificial inflation in VMware's stock price, repeatedly selling their shares in FY 2020 prior to each disclosure of declining backlog. Between June 4, 2019 and August 2, 2019 (the close of Q2 2020), the Company's executives sold an additional 84,053 shares of VMware stock at inflated prices for \$14.6 million in proceeds.

³ Pre-Class Period executive transactions include 11,167 shares of stock sold by Sybil Dawn Smith, VMware's former Senior Vice President, Chief Legal Officer and Chief Compliance Officer, in March 2017 for proceeds of just under \$1 million. Ms. Smith departed VMware in May 2017, and accordingly, had no Class Period transactions.

⁴ This included almost \$4 million in sales (21,086 shares) by defendant Gelsinger alone on March 1, 2019, the day after the Company's 4Q 2019 earnings call, and just three days before the Company issued a press release announcing the replacement of its Americas segment leader on March 4, 2019. See ¶¶44, 128, 130 above.

1 135. Between September 3, 2019 and November 1, 2019 (the close of Q3 2020), the
2 Company's executives sold an additional 81,547 shares of VMware stock at inflated prices for
3 proceeds of \$12.1 million.

4 136. After the close of Q3 2020 but before the Company announced its Q4 2020 results
5 including further declines in backlog, VMware executives sold an additional 48,158 shares of
6 VMware stock at inflated prices for proceeds of \$7.8 million.

7 137. The above stock sales were each close in time and proximity to the Company's Class
8 Period misrepresentations and partial disclosures of declining backlog and were made while the
9 executives were in possession of material nonpublic information obtained within the scope of
10 running the Company's day-to-day operations. By selling the above VMware shares, defendants
11 Gelsinger and Rowe and the other VMware executives were able to avoid the significant losses in
12 share value that followed from the disclosure of declining backlog. VMware executives sold
13 substantial amounts of their VMware shares at artificially inflated prices before the full truth about
14 VMware's misleading practices was revealed.

15 138. Throughout the Class Period, VMware's financial operations were overseen by
16 defendants Gelsinger and Rowe. They also repeatedly spoke on investor conference calls with
17 analysts concerning the Company's financial results. Defendants Gelsinger and Rowe had in place
18 extensive processes to track VMware's financial performance, including backlog, on a daily,
19 quarterly, and yearly basis.

20 139. Backlog is widely recognized by industry analysts as an important leading metric for
21 investors, and was a fundamental and central part of VMware's operations, as it was used to help
22 inform the magnitude of sales the Company had already secured, the revenue from which would be
23 recognized in subsequent quarters. At the end of FY 2019, the Company's total backlog and license
24 backlog were \$449 million and \$147 million, respectively. The backlog numbers were inflated at the
25 direction of management as employees were instructed to push sales orders into future quarters once
26 the Company had recorded enough revenue in order to meet current period guidance. As a result the
27 Company both reduced the amount of revenue required to meet FY 2020 revenue guidance and
28 obtained a head start toward meeting that guidance.

140. At the end of FY 2019, total backlog, which the Company disclosed as revenue it expected to likely recognize the subsequent quarter, constituted 20% of the Company's anticipated Q1 2020 total revenue. Likewise, license backlog at the end of FY 2019 represented 17% of the Company's license revenue guidance for Q1 2020. By the end of the Class Period these numbers had fallen to 0.7% and approximately 0.4% of quarterly total revenue and license revenue, respectively.

141. VMware's Chief Accounting Officer, who had signed each quarterly and annual report filed with the SEC from August 2018 through December 2019, abruptly resigned from VMware after six years of service, the same month the SEC began its investigation into the Company's accounting for backlog and related disclosures.

142. Given their roles as CEO and CFO of the Company, defendants Gelsinger and Rowe had access to material adverse non-public information about Company performance and the improper, unsustainable business practice of VMware deferring revenue not required to meet current period guidance into backlog so that it could be recognized in subsequent periods.

VII. LOSS CAUSATION AND ECONOMIC LOSS

143. The market for VMware's common stock was open, well-developed and efficient at all relevant times. Throughout the Class Period, VMware's common stock traded at artificially inflated prices as a direct result of defendants' materially misleading statements and omissions of material fact, which were widely disseminated to the securities market, investment analysts, and the investing public. Because defendants failed to disclose the true state of the Company's backlog and revenue, investors were not aware of the true state of the Company's operations as they were provided with a misleading picture of VMware's business. Lead Plaintiff and other members of the Class purchased or otherwise acquired VMware common stock relying upon the integrity of the market price for VMware's common stock and market information relating to VMware, and suffered economic loss, *i.e.*, damages, under the federal securities laws as detailed below and in §§IV.E-F, *supra*.

144. On May 30, 2019, after the market closed, VMware held a conference call to discuss its financial results for Q1 2020, as well as its business outlook for FY 2020. During the earnings

1 call, defendants *disclosed a significant decline in the Company's license backlog of over 67% from*
 2 *Q4 2019*. And, despite continued assurances previous quarters (including on February 28, 2019) that
 3 the Company was experiencing strength in each of its three geographical areas, defendant Gelsinger
 4 disclosed during the Q1 2020 conference call that “the Americas trailed” the Company’s other
 5 regional segments and was performing weaker than anticipated due to the departure of the region’s
 6 leader in February 2019, resulting in “territory realignments” and “adjustments to the
 7 org[anization],” which negatively affected the revenue recognized in that region. VMware’s stock
 8 dropped over 7% in the trading day following the Company’s May 30, 2019 disclosure. The same
 9 day, the S&P 500 index declined just over 1%.

10 145. VMware’s stock price continued to fall in tandem with the Company’s disclosures of
 11 declining backlog throughout the Class Period.

12 146. On August 22, 2019, the Company held its earnings conference call for analysts and
 13 investors. During that call, defendants again disclosed a substantial decrease in backlog – this time
 14 revealing that the Company’s *total backlog plummeted from a Class Period high of \$449 million at*
 15 *the end of FY 2019 to \$117 million at the close of Q2 2020 – a decline of 35% from the prior*
 16 *quarter and a 74% drop from just six months prior*. The Company also announced a *73% decline*
 17 *in license backlog from the previous quarter – to end with just \$13 million*, signaling weakened
 18 demand for the Company’s products. Defendants also *decreased* the Company’s license revenue
 19 guidance for the second half of FY 2020. Though defendants repeatedly assured investors during the
 20 Class Period that the Company was fully managing the industry-shift to subscription and SaaS
 21 products, defendants attributed the lowered full FY 2020 guidance to precisely that – the incremental
 22 mix shift toward subscription and SaaS. Following this news, the Company’s stock price fell over
 23 \$12 per share – a decline of 10% in one trading day. The same day, the S&P 500 index decreased
 24 just 2.5%.

25 147. On November 26, 2019, after the market closed, defendants held an earnings
 26 conference call for analysts and investors to disclose the Company’s Q3 2020 results. During that
 27 call, defendants announced yet another significant reduction in the Company’s total backlog – a drop
 28 of 39% from Q2 2020, to end the quarter at just \$71 million. In just nine months, VMware’s total

1 backlog fell over 84%. Following this announcement, VMware’s stock price fell nearly 6% in the
2 two trading days following the disclosure, while the S&P 500 was unchanged during the same
3 period.

4 148. On February 27, 2020, one year after VMware posted record-breaking backlog,
5 VMware’s backlog scheme finally unraveled. Defendants admitted that the Company was unable to
6 meet license and total revenue guidance *despite* the substantial backlog it had entering FY 2020.
7 Defendants announced a dismal \$18 million in total backlog and just \$5 million in license backlog –
8 a staggering decline of 96% and 97% to total backlog and license backlog, respectively, from the
9 inflated backlog reported at the end of FY 2019. As explained by defendant Rowe, the Company’s
10 backlog was a driver for the disappointing results as “in Q4 last year, we had . . . strong backlog that
11 we were able to utilize.” Thus, defendant Rowe admitted that lower-than-expected FY 2020 revenue
12 numbers were the result of among other things the Company’s inability to continue to draw on its
13 backlog as it had in prior periods.

14 149. To make matters worse, in a Form 8-K filed with the SEC the same day, the
15 Company revealed it was subject to an ongoing SEC investigation into the Company’s backlog of
16 unfilled orders. Specifically, the Form 8-K advised investors that, “[i]n December 2019, the staff of
17 the Enforcement Division of the [SEC] requested documents and information related to VMware’s
18 backlog and associated accounting and disclosures.” The Form 8-K also advised investors that,
19 although “VMware is fully cooperating with the SEC’s investigation,” it was “unable to predict the
20 outcome of this matter at this time.”

21 150. Defendants further revealed – after regularly remarking over the course of the prior
22 six quarters that the Company was weathering the industry shift away from license products in favor
23 of subscription and SaaS products – that the Company was in fact *not* successfully managing the
24 shift from license to subscription and SaaS revenue well. During the earnings conference call on
25 February 27, 2020, defendant Gelsinger stated that “revenue came in a bit short of expectations due
26 to a higher mix of subscription and SaaS.” The Company failed to meet its license revenue growth
27
28

1 targets for both Q4 2020 and FY 2020, and missed the Q4 2020 license revenue guidance defendants
2 issued just three months prior by 5%.⁵

3 151. The Company's stock price plummeted on the Company's February 27, 2020 news,
4 closing at a 52-week low of \$120.52 per share the next day – a one-day decline of over 11%, and
5 startling decline of \$85 per share or 41% – from the Class Period high reached during Q1 2020. The
6 same day, the S&P 500 index saw a decline of less than 1%.

7 152. In an analyst report issued the next day, Deutsche Bank called VMware's results
8 "disappointing," and "a messy and uninspiring print."

9 153. The declines in the price of VMware stock after each corrective disclosure came to
10 light were a direct result of the nature and extent of defendants' fraudulent misrepresentations and
11 omissions and the impact of the truth being revealed to investors and the market and were a
12 substantial cause of the declines. The timing and magnitude of the price declines in VMware's stock
13 compared to the market negates any inference that the loss suffered by Lead Plaintiff and other
14 members of the Class was caused by changed market conditions, macroeconomic or industry factors,
15 or Company-specific facts unrelated to defendants' fraudulent conduct. The economic loss, *i.e.*,
16 damages, suffered by Lead Plaintiff and other members of the Class was a direct result of
17 defendants' fraudulent scheme to artificially inflate the price of VMware's stock and the subsequent
18 decline in the value of VMware's stock when defendants' prior misrepresentations, omissions and
19 other fraudulent conduct were revealed.

20 **VIII. APPLICABILITY OF THE PRESUMPTION OF RELIANCE**

21 154. At all relevant times, the market for VMware stock was an efficient market for the
22 following reasons, among others:

23 (a) VMware met the requirements for listing and was listed and actively traded on
24 the NYSE, a highly efficient, electronic stock market;

25
26
27 ⁵ Defendants' guidance did not factor in amounts for the then-pending Pivotal acquisition, which
28 was completed in Q4 2020. Accordingly, for comparative purposes, reported revenue amounts used
herein to compare to guidance also exclude Pivotal.

(b) as a regulated issuer, VMware filed periodic public reports with the SEC and the NYSE;

(c) VMware regularly communicated with public investors via established market communication mechanisms, including the regular dissemination of press releases on national circuits of major newswire services and other wide-ranging public disclosures, such as communications with the financial press and other similar reporting services;

(d) VMware was followed by securities analysts employed by major brokerage firms who wrote reports that were widely distributed. Each of these reports was publicly available and entered the public market place; and

(e) VMware's stock price reacted in response to new material about VMware's business.

155. As a result of the foregoing, the market for VMware stock promptly digested current information regarding VMware from all publicly available sources and reflected such information in the price of the stock. Under these circumstances, all purchasers of VMware stock during the Class Period suffered similar injury through their purchase of VMware stock at artificially inflated prices and a presumption of reliance applies.

IX. CLASS ACTION ALLEGATIONS

156. Lead Plaintiff brings this action as a class action pursuant to Federal Rules of Civil Procedure 23(a) and (b)(3) on behalf of a class consisting of all persons who purchased VMware common stock during the Class Period and were harmed thereby (the "Class"). Excluded from the Class are defendants and their immediate families, the officers and directors of the Company, at all relevant times, members of their immediate families, and their legal representatives, heirs, successors or assigns, and any entity in which defendants have or had a controlling interest.

157. The members of the Class are so numerous that joinder of all members is impracticable. Throughout the Class Period, VMware shares were actively traded on the NYSE. While the exact number of Class members is unknown to Lead Plaintiff at this time and can only be ascertained through appropriate discovery, Lead Plaintiff believes that there are thousands of members of the proposed Class, if not more. Record owners and other members of the Class may be

1 identified from records maintained by VMware, its transfer agent or securities' brokers, and may be
2 notified of the pendency of this action electronically or by mail, using the form of notice similar to
3 that customarily used in securities class actions.

4 158. Lead Plaintiff's claims are typical of the claims of the members of the Class as all
5 members of the Class were similarly affected by defendants' wrongful conduct in violation of
6 federal law complained of herein.

7 159. Lead Plaintiff will fairly and adequately protect the interests of the members of the
8 Class and has retained counsel competent and experienced in class action and securities litigation.

9 160. Common questions of law and fact exist as to all members of the Class and
10 predominate over any questions solely affecting individual members of the Class. Among the
11 questions of law and fact common to the Class are:

12 (a) whether the federal securities laws were violated by defendants' acts as
13 alleged herein;

14 (b) whether statements made by defendants to the investing public during the
15 Class Period misrepresented material facts about the business and operations of VMware;

16 (c) whether the price of VMware stock was artificially inflated during the Class
17 Period; and

18 (d) to what extent the members of the Class have sustained damages and the
19 proper measure of damages.

20 161. A class action is superior to all other available methods for the fair and efficient
21 adjudication of this controversy since joinder of all members is impracticable. Furthermore, as the
22 damages suffered by individual Class members may be relatively small, the expense and burden of
23 individual litigation make it impossible for members of the Class to individually redress the wrongs
24 done to them. There will be no difficulty in the management of this action as a class action.

COUNT I

**For Violation of §10(b) of the Exchange Act and Rule 10b-5
(Against All Defendants)**

162. Lead Plaintiff repeats and re-alleges every allegation contained above as if set forth herein.

163. This Count is brought by Lead Plaintiff on behalf of itself and the Class.

164. This Count is brought against VMware and all Individual Defendants.

165. During the Class Period, each of the defendants named in this Count disseminated or approved the false statements specified above, which they knew or recklessly disregarded were misleading in that they contained misrepresentations and failed to disclose material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading.

166. Defendants violated §10(b) of the Exchange Act and Rule 10b-5 in that they:

(a) Employed devices, schemes and artifices to defraud;

(b) Made untrue statements of material facts or omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or

(c) Engaged in acts, practices, and a course of business that operated as a fraud or deceit upon plaintiff and others similarly situated in connection with their purchases of VMware stock during the Class Period.

167. Defendants, individually and together, directly and indirectly, by the use, means and instrumentalities of interstate commerce and/or the mails, engaged and participated in a continuous course of conduct to conceal the truth and/or adverse material about VMware's business, operations, and financial condition as specified herein.

168. Defendants had actual knowledge of the misrepresentations and omissions of material fact set forth herein, or recklessly disregarded the true facts that were available to them.

169. As a result of the dissemination of the materially false or misleading information and/or failure to disclose material facts, as set forth above, the market price of VMware common

1 stock was artificially inflated during the Class Period. In ignorance of the fact that the market price
 2 of the Company's common stock was artificially inflated, and relying directly or indirectly on the
 3 false and misleading statements, or upon the integrity of the market in which the Company's
 4 common stock traded, and/or on the absence of material adverse information that was known to or
 5 recklessly disregarded by defendants (but not disclosed in defendants' public statements during the
 6 Class Period), Lead Plaintiff and the other Class members purchased VMware common stock during
 7 the Class Period at artificially high prices and were damaged thereby.

8 170. Lead Plaintiff and the Class, in reliance on the integrity of the market, paid artificially
 9 inflated prices for VMware common stock, and suffered losses when the relevant truth was revealed.
 10 Lead Plaintiff and the Class would not have purchased VMware common stock at the prices they
 11 paid, or at all, if they had been aware that the market price had been artificially and falsely inflated
 12 by these defendants' misleading statements.

13 171. As a direct and proximate result of these defendants' wrongful conduct, Lead Plaintiff
 14 and the other Class members suffered damages in connection with their Class Period transactions in
 15 VMware common stock.

16 172. By reason of the foregoing, defendants have violated §10(b) of the Exchange Act and
 17 SEC Rule 10b-5.

18 **COUNT II**

19 **For Violations of §20(a) of the Exchange Act** 20 **(Against the Individual Defendants)**

21 173. Lead Plaintiff repeats and re-alleges every allegation contained above as if set forth
 22 herein.

23 174. This Count is brought by Lead Plaintiff on behalf of itself and the Class.

24 175. This Count is brought against the Individual Defendants.

25 176. The Individual Defendants were each control persons of VMware during the Class
 26 Period by virtue of their positions as senior officers of VMware.

27 177. Each of the defendants named in this Count acted as a controlling person of VMware
 28 within the meaning of §20(a) of the Exchange Act. By virtue of their high-level positions as officers

1 and/or directors of VMware, their ownership and contractual rights, participation in and awareness
 2 of the Company's operations, and intimate knowledge of the statements filed by the Company with
 3 the SEC and/or disseminated to the investing public, these defendants had the power to influence and
 4 control and did influence and control, directly or indirectly, the decision-making of the Company,
 5 including the content and dissemination of the allegedly false and misleading statements.

6 178. In particular, each of these defendants had direct or supervisory responsibility over
 7 the day-to-day operations of the Company and, therefore, is presumed to have had the power to
 8 control or influence the particular transactions and business practices giving rise to the securities
 9 violations as alleged in Count I, and exercised that power.

10 179. As a direct and proximate result of these defendants' wrongful conduct, Lead Plaintiff
 11 and other members of the Class suffered damages in connection with their purchases of the
 12 Company's common stock during the Class Period when the relevant truth was revealed.

13 180. By reason of the foregoing, the defendants named in this Count violated §20(a) of the
 14 Exchange Act.

15 **COUNT III**

16 **For Violations of §20A of the Exchange Act** 17 **(Against Defendant Gelsinger)**

18 181. Lead Plaintiff repeats and re-alleges every allegation contained above as if set forth
 19 herein.

20 182. This Count is brought by Lead Plaintiff on behalf of itself and the members of the
 21 Class who purchased VMware common stock contemporaneously with defendant Gelsinger's sales
 22 of VMware common stock.

23 183. This Count is brought against defendant Gelsinger.

24 184. During the Class Period, defendant Gelsinger was privy to confidential information
 25 concerning VMware's backlog, operations, finances, financial condition, and future business
 26 prospects, including, but not limited to, the false statements disseminated to the investing public.
 27 Notwithstanding his duty to refrain from trading in VMware common stock without disclosing the
 28 foregoing materially adverse facts, and in violation of his fiduciary duties to Class members,

1 defendant Gelsinger sold VMware common stock contemporaneously with Lead Plaintiff's purchase
2 and the purchases of VMware common stock by other Class members.

3 185. On March 1, 2019, the day after the Company disclosed record-breaking license
4 backlog, defendant Gelsinger sold 21,086 shares of his VMware stock at prices as high as \$181.61
5 per share for proceeds of \$3.77 million. Four days later on March 5, 2019, Lead Plaintiff bought
6 shares of VMware common stock. *See* Certification Pursuant to Federal Securities Laws, attached
7 hereto. Defendant Gelsinger sold his VMware shares as alleged above at prices artificially inflated
8 by the non-disclosure of material adverse non-public facts and misrepresentations of fact made
9 during the Class Period.

10 186. Defendant Gelsinger was aware that he was in possession of material adverse
11 information that was not known to the investing public, including Lead Plaintiff and other members
12 of the Class. Defendant Gelsinger was obligated to disclose the material nonpublic adverse
13 information to Lead Plaintiff and other members of the Class before selling his stock.

14 187. By reason of the foregoing, defendant Gelsinger directly and indirectly, by use of the
15 means and instrumentalities of interstate commerce, electronic communications, mailings and the
16 facilities of a national securities exchange, employed devices, schemes, and artifices to defraud and
17 engaged in acts and transactions and a course of business that operated as a fraud or deceit upon
18 members of the investing public who purchased VMware common stock contemporaneously with
19 the sales by the defendant named in this Count.

20 188. As a result of the foregoing, Lead Plaintiff and the other members of the Class who
21 purchased VMware common stock contemporaneously with the sale of VMware common stock by
22 defendant Gelsinger have suffered substantial damages measured by the amount of profits gained or
23 losses not incurred by reason of defendant Gelsinger's stock sales.

24 189. This action was commenced within five years after defendant Gelsinger made his
25 sales while in the possession of material non-public adverse information.

26 190. By reason of the foregoing, defendant Gelsinger violated §20A of the Exchange Act.

27 **PRAYER FOR RELIEF**

28 WHEREFORE, Lead Plaintiff prays for relief and judgment, as follows:

CONSOLIDATED COMPLAINT FOR VIOLATIONS OF THE FEDERAL SECURITIES

LAWS - 5:20-cv-02182-EJD

Cases\4828-0858-8233.v1-9/18/20

1 A. Determining that this action is a proper class action by certifying Lead Plaintiff as
2 Class representative under Rule 23 of the Federal Rules of Civil Procedure and Lead Plaintiff's
3 counsel as Lead Counsel;

4 B. Awarding compensatory damages in favor of Lead Plaintiff and the other Class
5 members against all defendants, jointly and severally, for all damages sustained as a result of
6 defendants' wrongdoing, in an amount to be proven at trial, including interest thereon;

7 C. Awarding Lead Plaintiff and the Class their reasonable costs and expenses incurred in
8 this action, including counsel fees and expert fees; and

9 D. Awarding injunctive and such other equitable relief as the Court may deem just and
10 proper.

11 **JURY DEMAND**

12 Lead Plaintiff hereby demands a trial by jury.

13 DATED: September 18, 2020

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26 Lead Counsel for Lead Plaintiff
27
28

CERTIFICATION PURSUANT TO FEDERAL SECURITIES LAWS

NORTHEAST CARPENTERS PENSION FUND (“Plaintiff”) declares:

1. Plaintiff has reviewed the consolidated complaint and authorized its filing.
2. Plaintiff did not acquire the security that is the subject of this action at the direction of plaintiff’s counsel or in order to participate in this private action or any other litigation under the federal securities laws.
3. Plaintiff is willing to serve as a representative party on behalf of the class, including providing testimony at deposition and trial, if necessary.
4. Plaintiff has made the following transaction(s) during the Class Period in the securities that are the subject of this action:

<u>Security</u>	<u>Transaction</u>	<u>Date</u>	<u>Price Per Share</u>
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See attached Schedule A.

5. Plaintiff has not sought to serve or served as a representative party in a class action that was filed under the federal securities laws within the three-year period prior to the date of this Certification except as detailed below:

In re Newell Brands, Inc. Sec. Litig., No. 18-cv-10878 (D.N.J.)
In re EQT Corporation Sec. Litig., No. 19-cv-00754 (W.D. Pa.)

6. Plaintiff will not accept any payment for serving as a representative party on behalf of the class beyond the Plaintiff’s pro rata share of any recovery,

except such reasonable costs and expenses (including lost wages) directly relating to the representation of the class as ordered or approved by the court.

I declare under penalty of perjury that the foregoing is true and correct.
Executed this 3rd day of September, 2020.

NORTHEAST CARPENTERS PENSION
FUND

By: 

Pete Tonia, Executive Funds Director

SCHEDULE A**SECURITIES TRANSACTIONS****Stock**

<u>Date Acquired</u>	<u>Amount of Shares Acquired</u>	<u>Price</u>
03/05/2019	396	\$173.29
05/07/2019	1,862	\$196.41
05/17/2019	353	\$204.62
05/30/2019	718	\$191.73
06/04/2019	626	\$173.13
07/11/2019	1,544	\$167.94
11/19/2019	10,500	\$172.02
11/27/2019	2,663	\$162.07
01/03/2020	21,488	\$154.06

<u>Date Sold</u>	<u>Amount of Shares Sold</u>	<u>Price</u>
09/07/2018	100	\$128.79
09/17/2018	1,200	\$132.92
11/14/2018	3,410	\$127.58
11/28/2018	834	\$130.68
12/07/2018	597	\$132.99
12/13/2018	497	\$135.31
12/18/2018	962	\$129.88

Prices listed are rounded up to two decimal places.

*Opening position of 7,600 shares.

CERTIFICATE OF SERVICE

I hereby certify under penalty of perjury that on September 18, 2020, I authorized the electronic filing of the foregoing with the Clerk of the Court using the CM/ECF system which will send notification of such filing to the e-mail addresses on the attached Electronic Mail Notice List, and I hereby certify that I caused the mailing of the foregoing via the United States Postal Service to the non-CM/ECF participants indicated on the attached Manual Notice List.

s/ SCOTT H. SAHAM
SCOTT H. SAHAM

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Mailing Information for a Case 5:20-cv-02182-EJD Lamartina v. VMware, Inc. et al**Electronic Mail Notice List**

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Manual Notice List

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- (No manual recipients)